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Bloomberg BusinessWeek

The End of Life

Lessons From a $618,616 Death

BY AMANDA BENNETT

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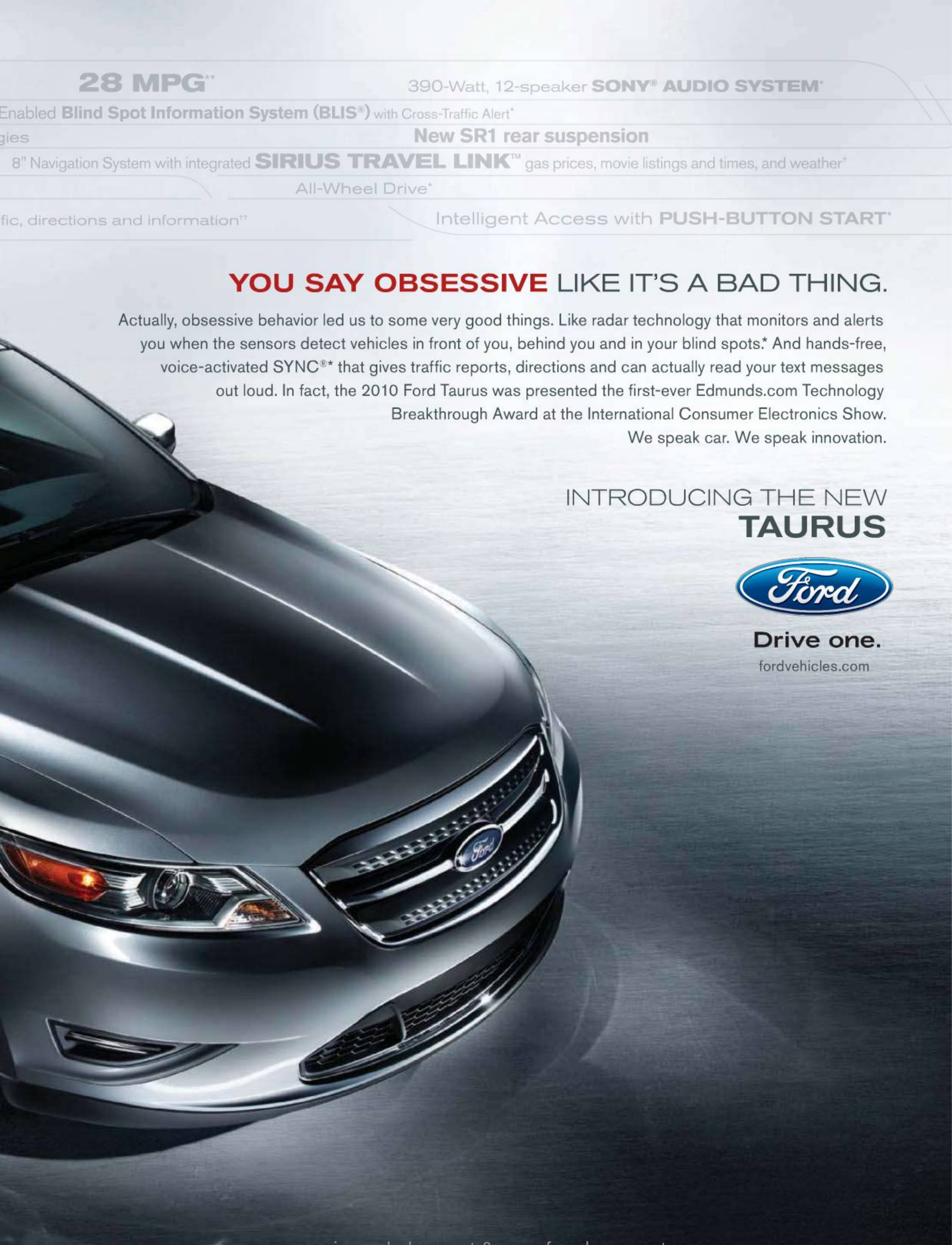
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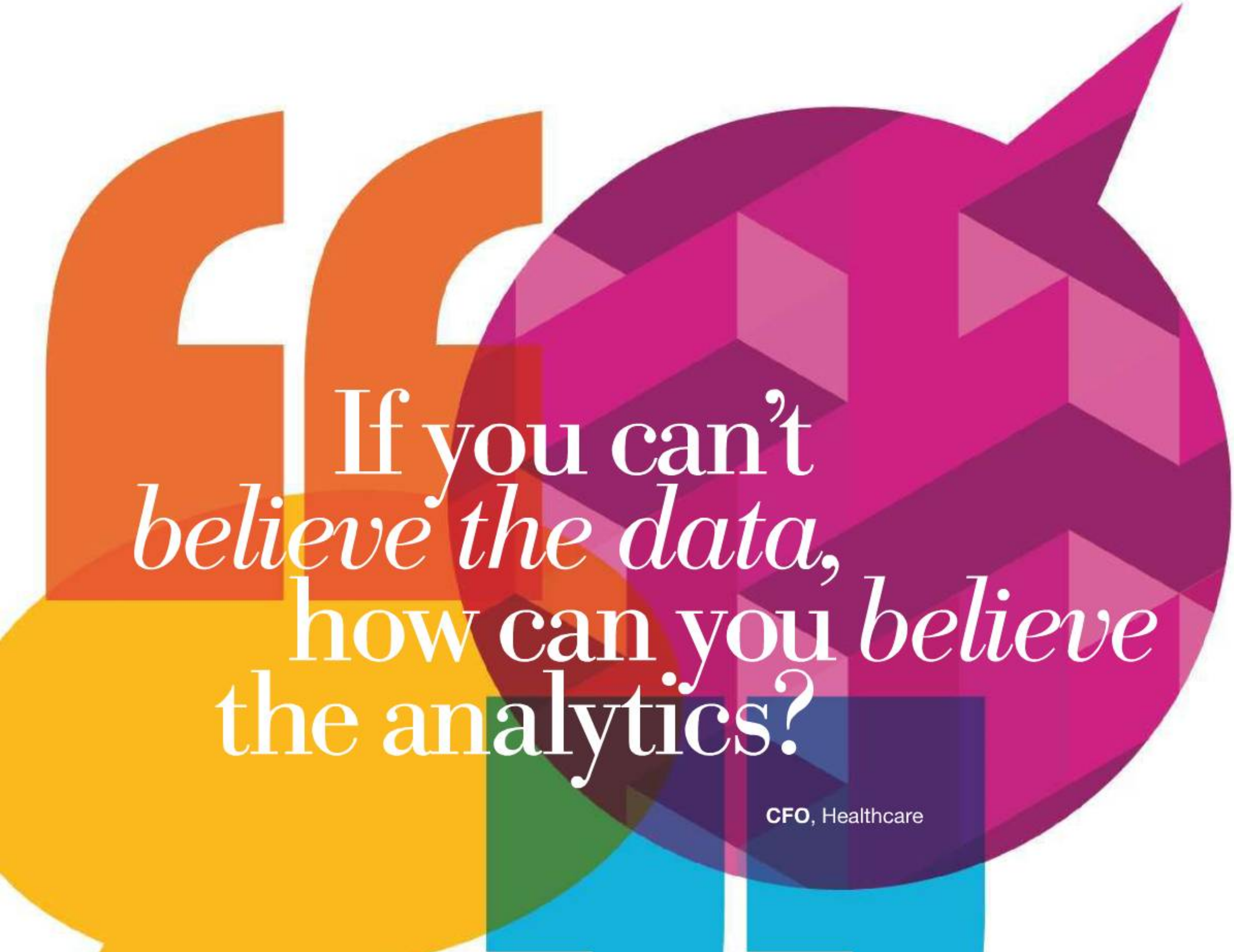
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Bloomberg BusinessWeek In Depth

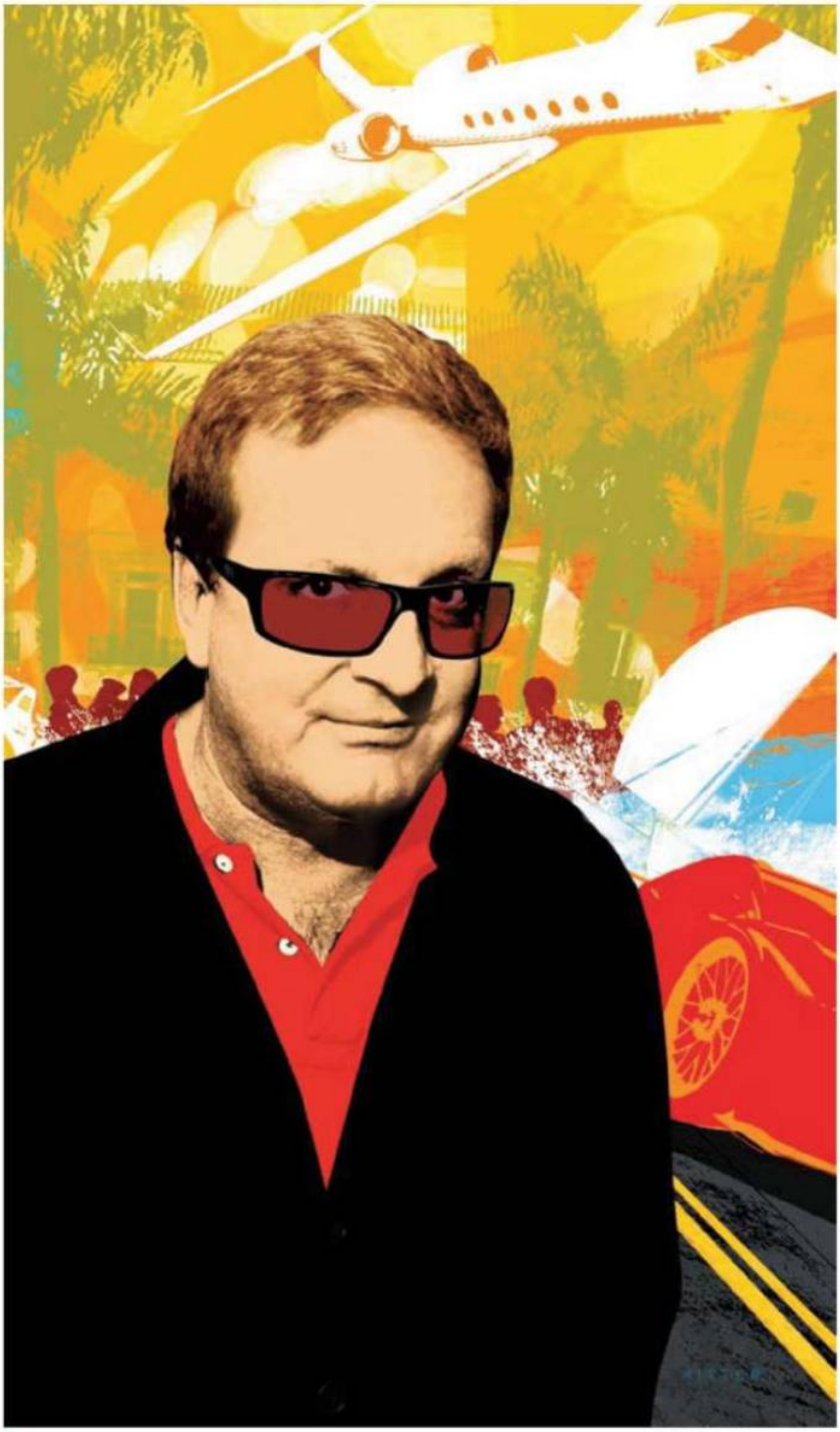


PHOTO ILLUSTRATION BY JOHN RITTER; PHOTOGRAPH BY A SCOTT/PATRICKMcMULLAN

Burkle's recent, activist investments are raising eyebrows

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When Amanda Bennett's husband was diagnosed with kidney cancer, she couldn't imagine that with the disease would come 5,000 pages of medical records. Two years after his death, her cover story examines the costs of keeping one man alive.

42 | The Other Ron Burkle

The billionaire investor, often dismissed as a playboy with a private jet, sold his portfolio before the roof caved in. Now he's buying into Barneys and Barnes & Noble—and gives his first interview in three years.

46 | A High-End Bet On Nuclear Power

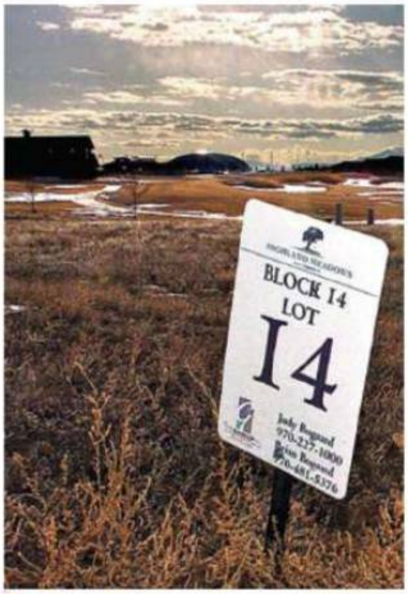
The CEO of French nuclear giant Areva, Anne Lauvergeon, says a bold new reactor design gives her company an edge over its competitors. With her job on the line, she's trying to drum up customers who can afford it.

50 | How Colleges Are Buying Respect

For-profit companies are scooping up small colleges to gain accreditation—and the financial aid dollars that come with it.

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Bloomberg BusinessWeek The Global Report



Land prices for housing are on the rise

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Chrysler's marketing gets a French twist



Richard Posner has had a change of heart

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(TOP) JENNY SPARKS/REPORTER-HERALD; (MIDDLE) DANIEL ACKER/BLOOMBERG; (BOTTOM) ROBYN TWOMEY/CORBIS OUTLINE

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Edited by
Harry Maurer and
Cristina Lindblad

THE WEEK IN BUSINESS



Rangel with House Speaker Nancy Pelosi: Will he be replaced permanently?

ECONOMICS & POLICY

FINANCIAL REFORM

The slow-motion ethics scandal chasing **Representative Charles Rangel** finally caught up with him. On Mar. 3 he announced he would temporarily step down as chairman of the tax-writing **House Ways & Means Committee.** The New York Democrat, a member of Congress since 1971, was scolded the previous week by the House for breaking rules on accepting gifts, and he remains under investigation by the **House Ethics Committee** for, among other things, allegedly failing to disclose income from a rental villa and enjoying the use of four rent-regulated apartments in Harlem. A House colleague told Bloomberg News that Rangel will be replaced for now by **California Representative Philip Stark,** a member since 1973. Expect a tussle over whether to replace Rangel permanently and with whom.

In other Washington news, **Senate Banking Committee Chairman Christopher Dodd** (D-Conn.) appeared to be nearing a compromise on financial reform. Dodd agreed on Mar. 1 to a proposal from **Senator Bob Corker** (R-Tenn.) that an agency to shield consumers from financial fraud be housed within the Fed rather than existing as an independent entity. Wall Street has been lobbying against a freestanding agency.

GREECE TIGHTENS AGAIN

Under intense pressure from bond vigilantes and the **European Union,** Greece cinched its belt one more time on Mar. 3, announcing a further $6.5 billion in budget cuts to tame its raging deficit. Vacation pay for government workers will be slashed by 30%, the value added tax will increase to 21% from 19%, and a grab-bag of other taxes will rise. The cutbacks helped soothe financial markets, which sent the euro to a 10-month low against the dollar on Mar. 2 amid talk of a bailout that might involve state-run banks buying Greek bonds. A day earlier the British pound also slid to its lowest point since May 2009 on fears of Britain's monster deficit.

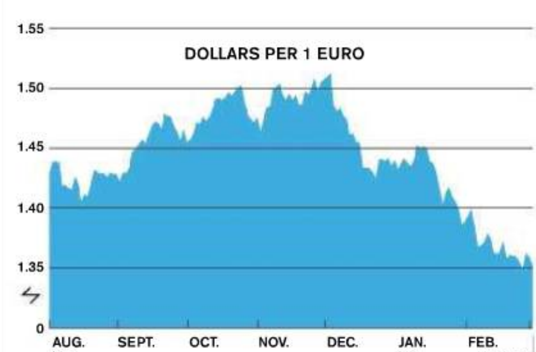
|BW| PAGE 24 "In Britain, a Rout Turns into a Race"

LEADERSHIP

A VACANCY AT THE FED

Fed Vice-Chairman Donald Kohn, a trusted adviser to

WEAKENING EURO



Data: Bloomberg

PHOTOGRAPH BY SCOTT J. FERRELL/CONGRESSIONAL QUARTERLY; CHART BY DAVID FOSTER/BW

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EXECUTIVE SUMMARY

Chairman Ben Bernanke and his predecessor, **Alan Greenspan,** said on Mar. 1 that he will step down in June after a 40-year Fed career. That gives **President Barack Obama** the chance to fill his seat as well as two other vacancies on the seven-member Board of Governors, which sets monetary policy and helps regulate the financial system. Bloomberg News reported that the White House contacted MIT economist **Peter Diamond** about filling one of the openings.

STRATEGY

BIOTECH BUYOUTS

The biotech sector was shaken up on Mar. 1 by takeover offers—one friendly, one not. Germany's **Merck** (not to be confused with Merck & Co., the U.S. pharma) said it would buy U.S. drug-technology provider **Millipore** for $6 billion in cash, or $107 a share, a 13% premium. Cancer-drugmaker **OSI Pharmaceuticals** received a hostile bid from Japan's **Astellas Pharma** of $3.5 billion, or $52 a share. Investors betting on a higher bid pushed OSI stock from 37 to 56. After OSI's board rejected the offer, Astellas filed suit, alleging that OSI wasn't acting in investors' best interests.



Lutz in Detroit: He sparked a design renaissance at GM with the Malibu and CTS

REBECCA COOK/REUTERS

LUTZ HITS THE OFF-RAMP

After 47 years in the car business, **General Motors Vice-Chairman Robert Lutz** announced his retirement on Mar. 3. The gravel-voiced executive, 78, had at least three acts. At Ford, he scored marketing victories in Europe by making the **Escort** a hot seller. He championed the flashy sports coupes and the **PT Cruiser** retro wagon that rejuvenated **Chrysler** in the 1990s. After joining GM on Sept. 1, 2001, he sparked an unexpected design renaissance with the **Chevrolet Malibu** and **Cadillac CTS.** In an unrelated move the company shook up its marketing staff. **GM-North America President Mark Reuss** cut out a layer of management by disposing of the general managers for each brand, though each division will have a sales and marketing boss. The move gives dealers a shorter line to Reuss. It also shows that the rising executive has the confidence of **Chairman and CEO Ed Whitacre Jr.** The company did hit one pothole this week: On Mar. 2, GM said it will recall 1.3 million compact cars because of power-steering problems.

"General Motors Executive Lutz Announces Plan to Retire May 1" businessweek.com/magazine



THE OPTIMISM METER

IS THE ECONOMY GETTING BETTER?

The Meter edged above 50 for the first time since mid-January, clocking in at 53 on Mar. 2. While only 25% of Americans think the economy is actually getting better, that's a vast improvement from a year ago, when just 9% were optimistic. Developed by ***Bloomberg BusinessWeek*** using data from pollster **YouGov,** the Meter is a proprietary measure of sentiment and expectations, economic statistics, and market forecasts. It evaluates shifts in outlook among individuals, professional investors, and economists in the areas of U.S. economic growth, jobs, equity markets, and real estate.

Calculated using consumer polling, economic forecasts, and financial markets data; 0=lowest and 100=highest Data: YouGov, *Bloomberg BusinessWeek*

AIG OFFLOADS A BIG ONE

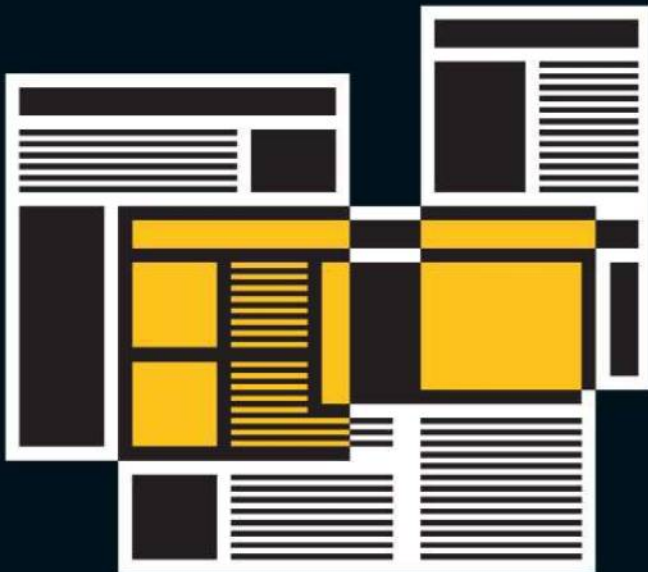
Cheer up, U.S. taxpayers: AIG is coming into some real money, and this time it's not from you. On Mar. 1, Britain's **Prudential** agreed to pay $35.5 billion in cash and stock for **American International Group's** Asian life insurance unit, **AIA Group.** The move boosts Prudential's

43.4%

Jump in Ford's U.S. vehicle sales in February, from a year ago. The increase pushed Ford past GM in monthly sales for the first time since 1998.

Data: Autodata

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EXECUTIVE SUMMARY



AIA in Singapore: AIG is selling the unit to Prudential for $35.5 billion

business in Asia and allows AIG to skip a time-consuming IPO it had been planning to launch for AIA. The biggest by far of 20 asset sales made by AIG since its $180 billion federal bailout, the deal provides a hefty premium over earlier bids. The **Federal Reserve Bank of New York** will get $25 billion of the proceeds when the deal is completed sometime this year. The noncash portion, $10.5 billion in Prudential securities, will be sold over time, and that money will also go to repay taxpayers.

TECHNOLOGY

APPLE TAKES OFF THE GLOVES

In the years since Apple launched the **iPhone** in 2007, **Google** has risen to become a dangerous, if distant, challenger with its **Android** phone software. Normally content to compete in the marketplace, Apple took an uncharacteristic step on Mar. 2 by seeking an injunction from the **U.S. International Trade Commission** that would stop phonemaker **HTC** from selling its Android-based models in America. Apple also sued HTC, claiming infringement of 10 patents including one related to the iPhone's multi-touch screen. Apple isn't going after Google directly, at least not yet—but this is only the latest shot in a rapidly escalating firefight.

IDEAS INTERNET CENSORSHIP: SHOWDOWN AT THE WTO?

The battle against China's Internet censorship may be moving to a new arena: the **World Trade Organization.** A Mar. 2 Bloomberg News report by **Mark Drajem** says the Obama Administration is weighing whether to file a WTO complaint against Beijing's Net restrictions on access and content, on the grounds that they discriminate against U.S. companies and online commerce. China is the world's biggest Internet market, with 384 million Web users at the end of 2009, according to the **China Internet Network Information Center,** which registers domain names.

Leading the charge are two industry groups with links to a roster of big-name American tech companies, including **eBay, Google, Microsoft,** and **Red Hat.** They are the **Computer & Communications Industry Assn.** and the **First Amendment Coalition. U.S. Trade Representative Ron Kirk** confirmed in a Feb. 23 interview with Bloomberg that his office is studying proposals submitted by the two groups.

Washington could have a tough time making the case that China's censorship rules hamper trade, say experts. "Censorship per se is not a violation of the WTO," notes **Warren Maruyama,** former general counsel of the U.S. Trade Representative's office. "You would have to show the violation of some specific WTO rule." Nor is a filing likely to lead to a speedy resolution. Disputes before the WTO can take two years or more to litigate and appeal.

Bloomberg News



Google's Beijing office: Its struggle with China could go to the WTO

(FROM TOP) VIVEK PRAKASH/REUTERS; NG HAN GUAN/AP PHOTO

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BUSINESS OUTLOOK | MIKE DORNING

SLASHING THE DEFICIT WITHOUT MASSIVE TAX HIKES

President Obama has asked a high-level commission to come up with ways to shrink the shortfall drastically by 2015. Doing so won't be painless ... but it's possible

For all the political theater surrounding the newly appointed deficit commission, there are some straightforward steps it could take to change the alarming U.S. debt dynamics. The panel is supposed to recommend ways to narrow the gap to 3% of gross domestic product by 2015, down from this year's 10.6%, and improve the fiscal outlook by tackling entitlement programs. Here's how it could be done:

Start with Social Security. Now on track to become insolvent by 2037, the program with modest changes could contribute $60 billion in annual savings by 2014. A quarter of the $5.3 trillion Social Security shortfall over the next 75 years could be made up simply by pegging annual cost-of-living adjustments made to retirees' pensions to an index many economists believe measures inflation more accurately than the one Washington uses. Adopting the so-called chained consumer price index—which takes into account people's tendency to substitute similar but cheaper products when prices rise—would save taxpayers billions.

$94.5 billion

The amount the U.S. government would save in 2014 by ending federal deductibility of state and local taxes

Data: Congressional Budget Office

People live longer now. Recognizing that, raising the retirement age would make up another quarter of the gap. The full Social Security retirement age is already rising to 67 for those born after 1959. Save big by including those born after 1958 and pushing the eligibility back by a month every other year. The retirement age still wouldn't reach 69 until long after today's workers retire.

The remaining shortfall could be gained from a tiny boost in the Social Security tax—four-tenths of a percent, split between workers and employers—and by lifting the cap on wages subject to the levy to $198,000 from today's $106,800.

As for the deficit in 2015, if the rosy economic assumptions in the Obama Administration budget are replaced with more realistic ones, $423 billion would have to be slashed from the White House's spending plan. The budget already counts on tapping the wealthy by allowing Bush-era tax cuts to expire for families earning more than $250,000 per year, raising current estate and capital gains taxes, and hitting up banks to recover the cost of the financial bailout. So the $423 billion needs to be cut elsewhere.

Again, an updated inflation index could be used. By switching all government programs, including federal pensions, and the tax code to the chained CPI, we'd save an additional $10 billion annually above the $60 billion gained from the Social Security fix.

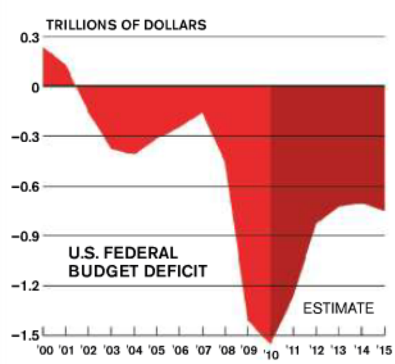
Now comes the politically hard part: limiting tax breaks dear to the middle class. End the deduction for state and local taxes. Cap the portion of home loans eligible for mortgage interest deduction at $500,000. Curb charitable giving deductions to cover only those above 2% of income. Limit the exclusion from taxes for employer-provided health coverage to $1,440 a month for a family plan. Plus, end the tax exclusion for employer-paid life insurance. In all, that would raise $161 billion.

A carbon tax similar to Obama's cap-and-trade emissions plan would raise $50 billion, even if half the revenue went to tax credits for low- and moderate-income families and aid to coal-mining towns and other affected communities. And an excise tax on sugar-sweetened drinks of a penny per ounce would raise $20 billion.

The President wants a three-year freeze on domestic discretionary spending. It has already been swelled by stimulus outlays, and surely by 2015 the recession will have passed. So reduce domestic discretionary spending to its inflation-adjusted, pre-stimulus level of 2008 for $43 billion in savings. A 20% drop in farm subsidies yields $3 billion more. And canceling just three big weapons programs—the Joint Strike Fighter, the Future Combat Systems, and the Maritime Prepositioning Force—would save $9.3 billion. The remaining $67 billion could be met by cutting an additional 5.4% of overall discretionary spending (11.9% if defense is excluded) or raising income tax rates by 1.4 percentage points.

Obviously, there's plenty not to like here. The point is that it's not impossible to fix the deficit. It just requires sacrifice. |BW|

NOTHING BUT RED INK ON THE HORIZON



Data: Office of Management & Budget

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NUMBERS

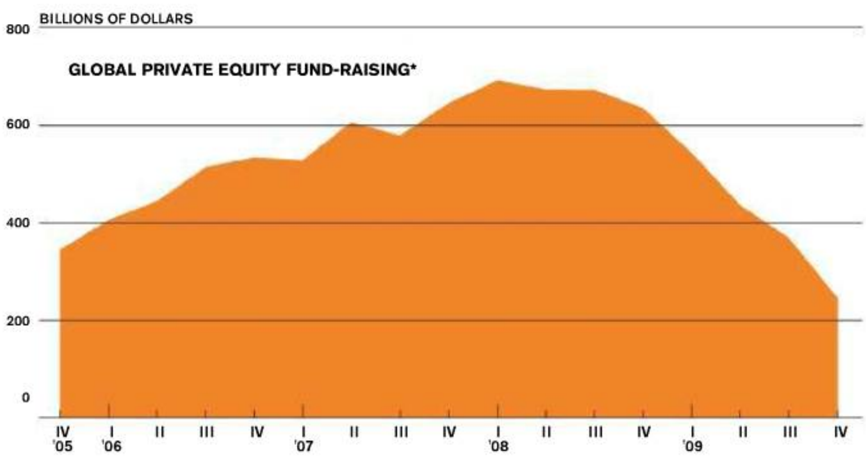
PRIVATE EQUITY: LESS ACTION, BETTER RESULTS

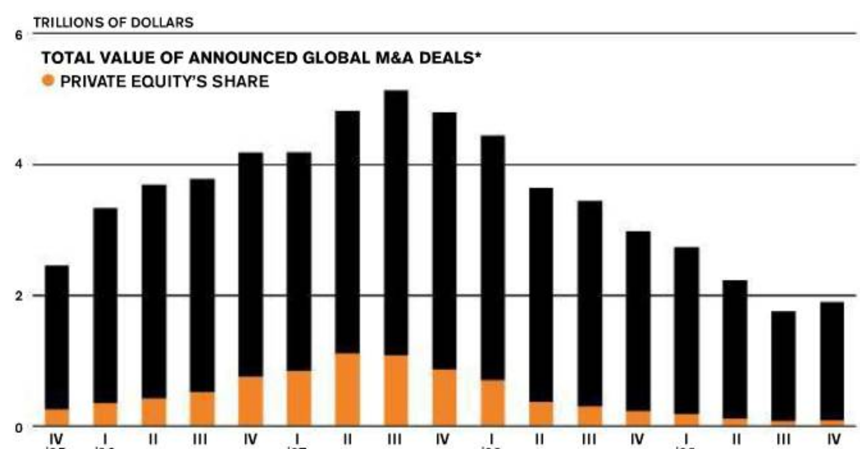
By Tara Kalwarski/Charts by David Foster

Investors cooled on private equity in 2009, with firms taking in just $246 billion in new funds globally—less than they have in each of the previous five years. But returns of private equity mostly topped U.S. stocks' performance in recent years. And big players like Blackstone Group have cash to deploy if they want to start cutting deals again.

FEWER FUNDS—AND DEALS

As inflows of investment dollars have dried up, private equity's share of global mergers and acquisitions has also shrunk considerably.



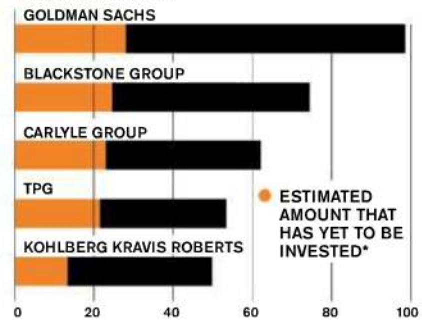


Data: Bloomberg, Preqin

*Rolling four-quarter sums

Fat Coffers: These big private equity players have a total of about $110 billion in funds still to invest.

FIRMS THAT HAVE RAISED THE MOST PRIVATE EQUITY MONEY OVER THE PAST 10 YEARS

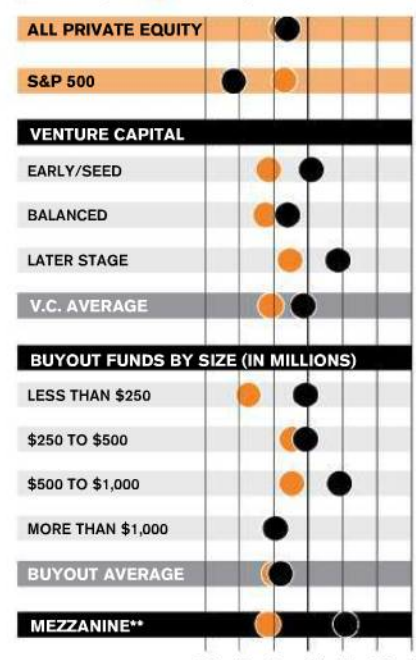


*Excludes fund of funds and secondary fund of funds
Data: Preqin

Performance Power: Private equity lost less than the S&P 500 in the two years ended Sept. 30, 2009.

HISTORICAL PERFORMANCE BY TYPE OF PRIVATE EQUITY INVESTMENT*

ONE-YEAR PERCENTAGE RETURN AS OF:
● SEPT. 30, '08 ● SEPT. 30, '09

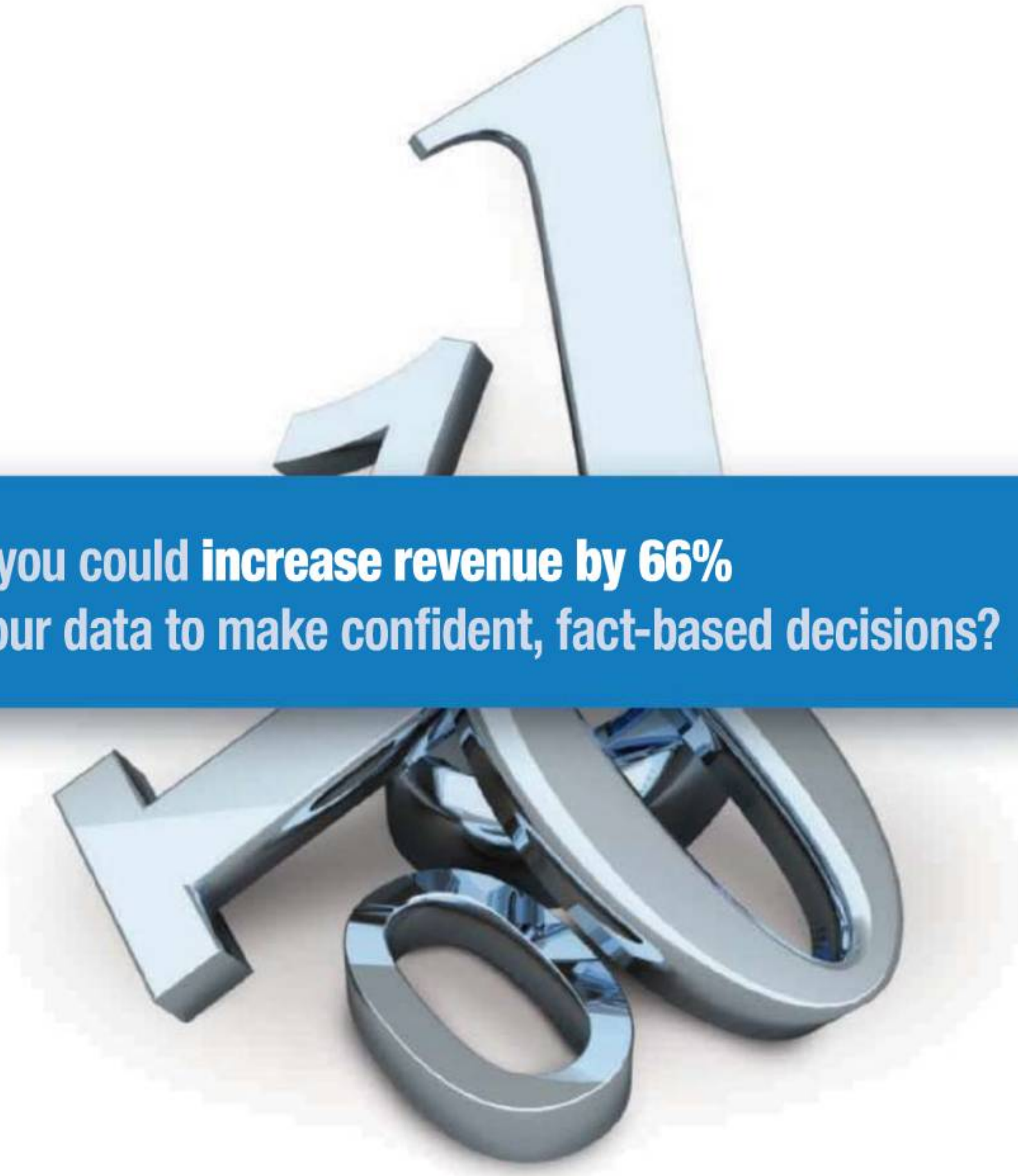


*Returns are net to investors after fees and carried interest
**Includes deals financed with subordinated debt or preferred equity
Data: Bloomberg, Thomson Reuters

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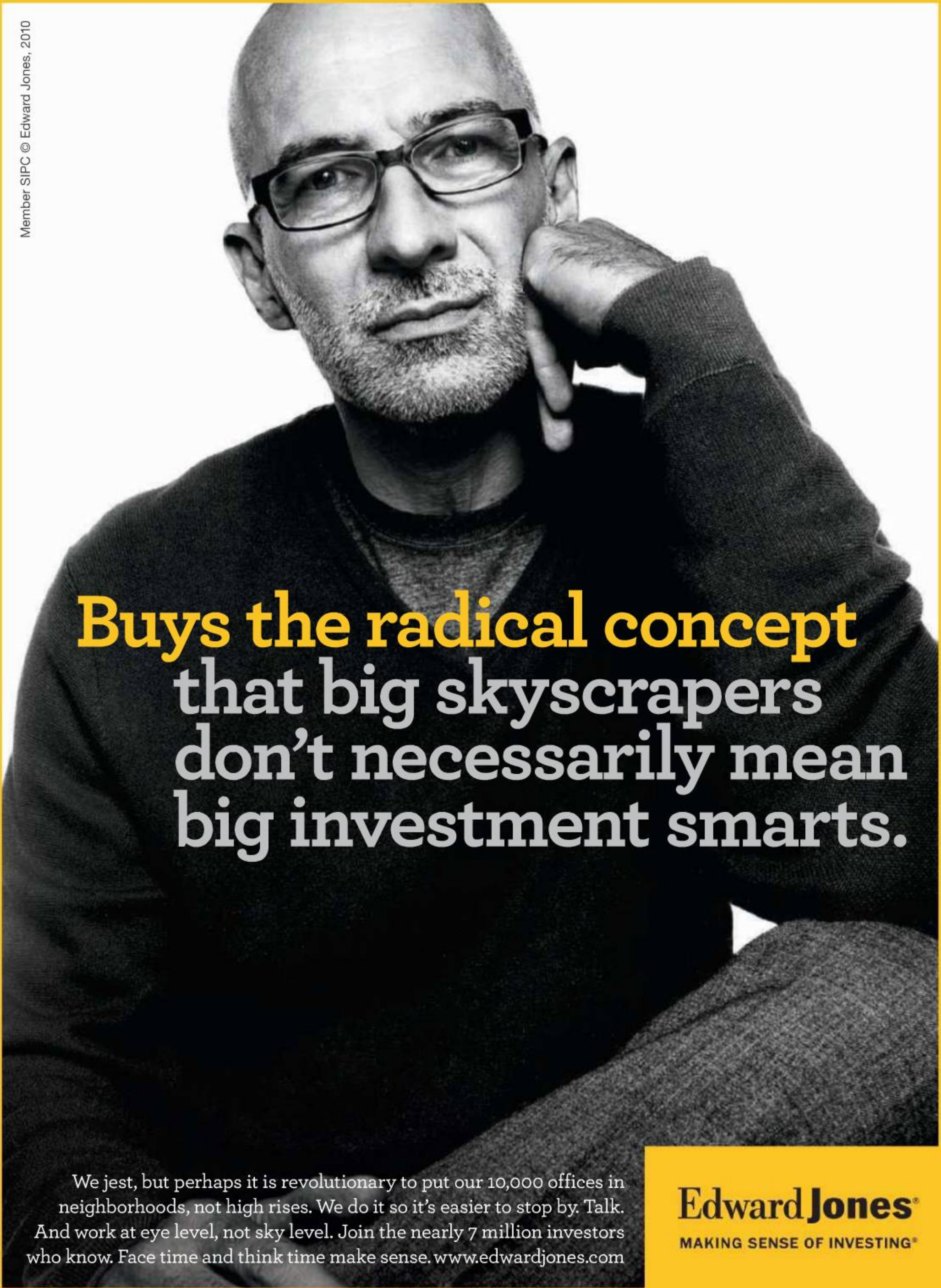
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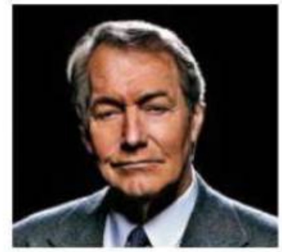
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AT THE TABLE CHARLIE ROSE





ELIZABETH WARREN
Outrage and Financial Reform

Harvard Law School Professor Elizabeth Warren is chair of the Congressional Oversight Panel, created in 2008 to monitor the Treasury Dept.'s bank bailout and to review the regulation of financial markets. With a compromise on financial-reform legislation looking imminent, I talked with Professor Warren on Mar. 3. Edited excerpts from that conversation follow.

(FROM TOP) BRAD TRENT; JEFFREY MACMILLAN

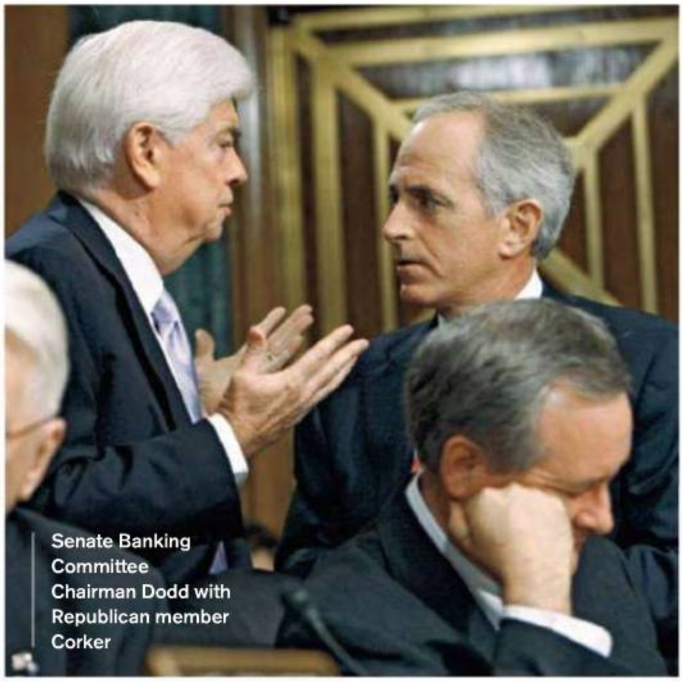
CHARLIE ROSE
Tell me what you think about the debate over a consumer protection agency. A House bill calls for an independent agency. Now you have Senators Chris Dodd and Bob Corker of the Banking Committee suggesting a compromise may put it inside the Federal Reserve.

ELIZABETH WARREN
This is less about real estate and more about genuine independence. So here's the deal: Right now the Fed has the power actually to do a lot of this. The Office of the Comptroller of the Currency, which is the federal bank regulator, has the power to do a lot of what this agency would do. But the truth is, they're not interested. It's not what they do.

Someone said monetary policy was in the penthouse and consumer protection was in the basement.
It's the stepchild nobody wants. There's nobody in Washington focused on the economics of the family, focused on the consumer products—credit cards, mortgages, car loans,

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overdraft fees. All the stuff you have to do in your daily life to survive economically. This is an industry where the business model has fundamentally changed. Back in 1980 the credit-card agreement for Bank of America would have fit on one sheet of paper. Terms were clear. They figured—well, here's your creditworthiness, and here's what we have to charge. We're a little worried about inflation, how much it's going to cost us to monitor this, so we'd better make a little profit. It worked, right? Mortgages were set up pretty much the same way; car loans, too. Then we got rid of usury laws. And the credit-card folks said, you know, we could just hold up one or two things in front of you: low, low financing—7.9%. We could hold up free gifts. We could hold up a warm and fuzzy relationship. And then we could put what are called in the trade revenue enhancers back in the fine print, and we could make a lot of money because you won't figure out what this product costs. So that one-page credit-card agreement in 1980 has now grown to about 30 pages. And it's not just 30 pages, it's 30 pages of incomprehensible fine print.



Senate Banking Committee Chairman Dodd with Republican member Corker

Even though you say it's not about real estate, do you have a preference where this agency should be?
Standing alone.

A whole new bureaucracy even though the Fed has the tools to start doing it tomorrow?
There are seven bureaucracies in Washington right now that each own a piece of consumer financial protection. Bloated, inefficient, and either ignored and ineffective or captured by the large financial institutions. [This is] the regulatory system we've got now. It works very well for the large financial institutions because it means no effective regulation. What I want is to take this agency out of those seven agencies, shrink it down, and make it effective. You've got to have an agency that's ultimately independent, whether it's located within the Fed, within Treasury, within the Department of Agriculture, or whether it sits in its own separate place. The key is whether or not it is functionally independent. Does it write its own rules? Does it enforce those rules and does it have access to a budget that's independent of the folks who want to smother it?

I DON'T CARE HOW BIG YOU ARE. … IF YOU MAKE BAD ENOUGH DECISIONS, YOU CAN BE LIQUIDATED

What do you think will happen?
Politics is already happening, Charlie. Let's be clear where we are. This is an agency that just makes sense. This isn't liberal or conservative. This isn't a division of ideology. This is about bank lobbyists. This is about people who are paid professionally to kill this agency so they can protect the revenues of Wall Street banks.

Are Dodd and Corker serving the interests of the bank lobby?
Well, we'll know when this bill comes out of Congress.

As part of overall financial reform, where do you put the significance of the agency?
The tip of the spear in the sense that this is where our financial crisis started: one lousy mortgage at a time; one family who got tricked, cheated at a time. Then those risks were sliced, diced, and put into all kinds of fancy financial instruments that made billions for Wall Street banks and then [crashed] the whole system.

Are you in favor of the so-called Volcker Rule that suggests commercial banks shouldn't engage in proprietary trading, owning hedge funds, owning private equity firms.
I like Volcker, but I think it has to be a little bigger. The idea behind it is if you're going to take deposits, if you're going to be one of our guaranteed institutions, then there is a range of interconnected financial activities that have to be more carefully examined: defaults and swaps and derivatives. We can't let a nonbank pull the whole game down.

What else do you want to see in a regulatory bill?
We started at families. The other end is too big to fail. [We need] a Chapter 11 system, whatever we want to call it, a part of the legal structure that permits us as a people to say with real credibility: I don't care what your business is. I don't care how big you are, how intertwined you are. If you make bad enough decisions, you can be liquidated. Your shareholders wiped out and top management fired. |BW|

Watch Charlie Rose on Bloomberg TV weeknights at 8 p.m. and 10 p.m.

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Housing: Hope On the Horizon

Cash-rich builders are buying land again, betting on a turn in the market for new homes

By Peter Coy and John Gittelsohn

You would think the nation's biggest homebuilders would be writhing in pain right about now. Sales of new single-family homes sank in January to the lowest seasonally adjusted rate in nearly five decades of record keeping and are now off 78% from the housing market's frothy peak in 2005.

Yet in a housing industry as vast and varied as America's, the data often fail to keep up with reality. It turns out that big publicly traded builders, thanks to cost-cutting, asset sales, bond issues, and tax breaks, aren't in grim shape. Their shares have nearly doubled over the past year and they're back in the game of competing for land, reflecting confidence that after years of falling prices, rising foreclosures, and busted dreams, better days are ahead.

The number of lots owned or controlled by a dozen of the biggest builders rose slightly in the second half of 2009 after years of decline as renewed buying offset heavy tax-related selling of unwanted parcels, according to a Bloomberg analysis of company reports. In crash-prone markets such as Southern California and Florida, prices of some construction-ready lots are up 50% or more from their 2009 lows. "There is definitely a shortage of land, and you cannot turn the switch on overnight," says Douglas C. Yearley Jr., executive-vice president of luxury builder Toll Brothers. "That will cause builders to aggressively buy the land they can."

Land buying began to pick up last year after finished lots hit the market at below the cost of improvements, and housing prices stabilized. Builders could finally turn out homes with some assurance of making a profit, says Scott D. Clark, the CEO of Americap Development Partners, a residential land developer in San Ramon, Calif. Greater affordability and tax incentives should help in the short term. What's more, the big builders believe population growth will eventually require a burst of construction. Warren Buffett agrees. In his Feb. 27 letter to shareholders of Berkshire Hathaway, which owns manufactured-housing maker Clayton Homes, he predicted that "within a year or so residential housing problems should largely be behind us."


JENNY SPARKS/REPORTER-HERALD

The builders are staying disciplined for now, selectively scooping up bargains while buying just what they need to meet expected demand for the next few years. "There isn't one public homebuilder that's stupid. They're all well-seasoned. They've shrunk down to the size they need to be, and now they're reacting accordingly" to op-

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One broker is shocked at the interest in Colorado lots like this one

portunities for growth, says James T. "Nate" Nathan, the president of Scottsdale (Ariz.)-based land broker Nathan & Associates.

It's tough to say how much land prices have risen because each market is different. Last year, DMB Associates, a developer in Scottsdale, and its partners bought back about 400 lots in DMB's Verrado master-planned community in Buckeye, Ariz., that builders had acquired and then defaulted on. They spent about $15,000 per lot, then quickly resold 300 of the lots to other builders for an average $40,000 per lot. Nationally, though, increases have been considerably smaller than that.

The uptick in prices matters because land is the main factor in real estate's roller-coaster cycle. When housing prices boomed in the middle of the last decade, it wasn't the structures that were suddenly deemed more valuable but the land. Economist Morris A. Davis of the University of Wisconsin-Madison School of Business estimates that the price of U.S. land used for houses and apartments nearly tripled from the beginning of 2000 to the end of 2005. Prices more than tripled over the period in Washington, Miami, Tampa, San Diego, Los Angeles, and

AFTER THE LAND CRASH, AN UPTICK



*Two-quarter moving average

Data: Morris Davis, University of Wisconsin-Madison; Lincoln Institute of Land Policy

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Arizona: DMB flipped some Verrado lots for a quick $25,000 apiece

BRENDAN MOORE

Phoenix, and better than quadrupled in two inland California markets, Sacramento and San Bernardino, Davis estimates. He figures that national land prices fell nearly two-thirds through early 2009 before bouncing back more than 20% in the rest of '09. (To calculate the implied value of land, he takes the fluctuating market value of residential properties and subtracts the relatively stable replacement cost of the structures on them.)

The sharp decline in land prices was especially hard on the small builders that account for about 70% of the market. The National Association of Home Builders says its membership has fallen by about 20%, or 45,000. Many that remain have slashed staff. Jerry Howard, CEO of the NAHB, says banks are refusing to extend credit to small builders and stiffening the terms on existing credit.

In contrast, most of the big builders whose shares are publicly traded are battle-hardened and ready to grow again. Writedowns and write-offs by 13 of the largest public builders exceeded $32 billion through December, according to Fitch Ratings. In contrast to small builders, which rely almost entirely on banks for financing, several big builders were able to raise funds by issuing bonds.

An additional boost came last year when Congress passed a law allowing companies to get refunds on past years' tax payments by applying their recent losses to earnings dating back five years. Many sold land at big losses to boost their refunds. The result was a windfall of $2.3 billion for the builders as a group, including $800 million for No. 1 Pulte Homes.

The result of those balance-sheet heroics? Builders have more than $12 billion in cash they can use to replenish their land inventory. Pulte and D.R. Horton each had $1.9 billion in cash and near-term equivalents at the end of December, Toll Brothers had $1.6 billion at the end of January, Lennar had $1.3 billion, and KB Home had $1.2 billion at the end of November.

Some of that cash is going for parcels that weaker builders lost through default or short sales. On Feb. 25, Starwood Land Ventures of Bradenton, Fla., announced it received "interest from nearly every major homebuilder in Florida" for about 5,400 residential lots it bought in the bankruptcy auction of Hollywood (Fla.)-based TOUSA, one of the few big builders that bit the dust. Lennar was first in line, agreeing with Starwood to acquire or get purchase options on more than 2,700 of the TOUSA lots across Florida. The price wasn't disclosed, but Lennar said it expects to earn gross margins of 20% or better on the deal. In Loveland, Colo., land broker Craig Harrison of Harrison Resource Corp. says he's "in shock and awe" at the amount of interest he's getting from builders and investors for 5,000 acres of land across northern Colorado that recently went on the market for $177 million.

Builders are buying land in part because the parcels they have aren't in the places where they need them. Property on the outer fringes of metro areas is still out of favor, says Daniel Oppenheim, a Credit Suisse homebuilding analyst. Prices have risen the most for closer-in lots that already have sewer lines, water, electricity, and sidewalks, because builders can throw up houses on them quickly and sign deals by Apr. 30 to qualify for federal homebuyer tax credits. Builders that aren't focused on a quick sales pop are choosing to buy cheaper "paper lots" that lack infrastructure, says Jody Kahn, vice-president of regional markets for Irvine (Calif.)-based John Burns Real Estate Consulting.

Interest in unfinished land usually comes later in the housing cycle, says Thomas E. Lucas, senior vice-president of operations for DMB in Scottsdale. "We didn't think we'd sell raw land for three to four years," Lucas says. That's a striking vote of confidence considering the threats to housing from high unemployment, rising mortgage rates, and foreclosures.

Everything seems to happen faster these days—including the housing cycle, which is heading up before it has hit bottom. BW

BIG BUILDERS HAVE RAISED BILLIONS, AND THEY CAN SNAP UP PROPERTIES THAT SMALLER RIVALS DEFAULTED ON

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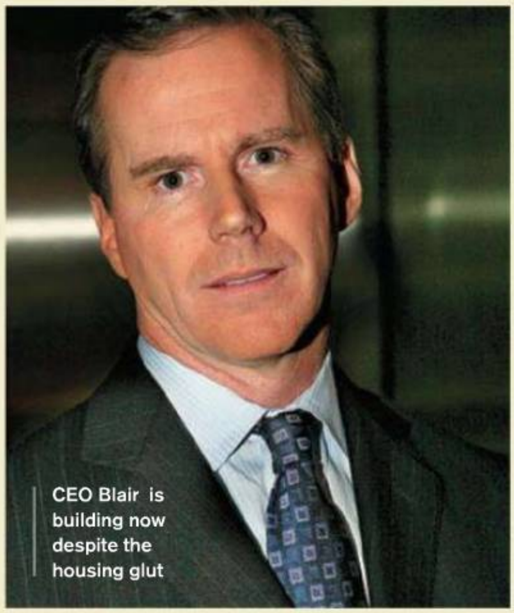
Getting Ahead of An Apartment Crunch

In the face of record vacancies and plunging rents, AvalonBay is starting to put up new buildings. Crazy or crazy-smart?

By Prashant Gopal

Kristin Davie misses her freedom. The 22-year-old has been living with her parents in Colonia, N.J., since graduating from Marist College in May. She and two friends set a deadline of September to find jobs and a New York City apartment they could afford to share. September's long gone, and she's still at home. Davie left her first job, where she was unhappy; now she has a new one. "I'm hoping we'll be in the city by the end of April," she says.

The managers of AvalonBay Communities are hoping right along with her. While most apartment construction is on hold, AvalonBay, a real estate investment trust based in Alexandria, Va., plans to start $400 million worth of new rental units this year, mainly in the Northeast.



CEO Blair is building now despite the housing glut

"IF WE'RE ABLE TO DELIVER NEW PRODUCT INTO A PERIOD THAT IS ABSENT OF SUPPLY, WE'LL HAVE AN ADVANTAGE"

With the unemployment rate at 9.7% and the apartment vacancy rate at 8%—the highest ever, according to research firm Reis—this might seem like the worst possible time to start building. Rents plunged last year, yet AvalonBay CEO Bryce Blair says it won't be long before the job market recovers and people in their twenties, such as Davie, move away from home or out of their shared apartments and into rentals of their own. The units AvalonBay plans to start this year won't be ready for occupancy until 2012, and by then Blair expects demand to be strong. "If we're able to build and deliver new product into a period that is really absent of supply," he says, "we'll have a competitive advantage."

With $300 million in cash and a $1 billion credit line, AvalonBay, the second-largest publicly traded apartment owner in the U.S., can afford to be contrarian. Construction financing for private developers—a category that includes most of AvalonBay's rivals—dried up as banks were swamped by bad loans. U.S. builders started 92,000 units in 2009, a 58% decline from 2008 and the fewest since the government began collecting the data in 1974. AvalonBay built nothing for the first nine months of last year, then started two projects.

"It is as difficult to finance a new development today as in any time in my 30 years in the real estate business," says Charles R. Brindell Jr., president and CEO of closely held Trammell Crow Residential, which has developed more than 225,000 multifamily units across the U.S. For the first time in its 33-year history, Trammell Crow didn't start a single development last year, when it failed to line up financing for four planned projects in the Northeast.

The largest publicly traded apartment owner, Equity Residential, the real estate investment trust founded by billionaire Sam Zell, is emphasizing acquisitions over construction. It does, though, plan to build 111 units on a property in the Chelsea neighborhood of Manhattan that it acquired in 2009.

RIVALS READY TO POUNCE

Will AvalonBay's bet pay off? Ron Witten, founder of Witten Advisors in Dallas, is a believer. "We will have fewer apartments than the market will have need for," he says, "which will drive rents higher." Witten says rents may increase by about 6.5% and the vacancy rate drop below 5% by 2012. Others think any shortage won't last long. "When financing gets better," says Victor Calanog, director of research at Reis, "building is going to be quick."

Certainly, some areas will rebound faster than others, and Kristin Davie may want to find a place soon. According to forecasts by research firm Axiometrics, New York City rents could climb 6.7% next year and 8.6% in 2012. |BW|

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In Britain, a Rout Turns into a Race

As the Tories talk tough about trimming the public sector, voters get nervous—and Labour suddenly has a chance

By Stanley Reed and Gonzalo Vina

No matter how uncertain life in Britain became during the global crash and its painful aftermath, one thing seemed sure: Prime Minister Gordon Brown and his Labour Party would get trounced in the next election. Since 2008, the opposition Conservatives have mostly enjoyed a double-digit lead in the polls.

With the election now expected in May, however, the expected rout is suddenly too close to call. A YouGov survey released on Feb. 28 had Labour trailing by just two percentage points, well within the margin of error. Other polls show the Tory lead down to five points, which pollsters doubt would give the Conservatives a clear majority.

That news just about spoiled the Conservatives' spring conference in Brighton. David Cameron, the still young (he's 43) but perhaps not quite so smoothly confident Tory leader (he has been waiting years for this moment), told the party faithful on Feb. 28 that he faced a "real fight" to unseat Brown. "We all know the British people have still got some big questions that they want to ask us," Cameron said.

The tightening race has spooked the currency markets by suggesting the possibility of a hung Parliament, with no party wielding the clout needed to deal with looming budget deficits. The YouGov poll triggered a 3% plunge in sterling over Mar. 1 and 2—11% off its November high—before the currency recovered slightly to $1.51. The Bloomberg consensus is for the pound to climb back to $1.64 by yearend.

How the Tories squandered their advantage is a matter of debate. Just about everyone agrees that the party's pronouncements on the economy, which shrank 4.8% in 2009, have played a big role. The Conservatives have been brutally frank on the need to rein in the budget deficit, projected at 12.6% of gross domestic product for this fiscal year. George Osborne, the party's choice for Chancellor of the Exchequer, wants an emergency budget within 50 days of the Tories' taking power that will freeze public sector pay, cut the cost of central government by 33% over five years, and boost the qualifying age for a pension. Whoever wins the election, he said on Feb. 25, "will have to be tougher than Margaret Thatcher."

David Cameron's Tory party has squandered a double-digit lead in opinion polls

The Iron Lady hasn't been Prime Minister for nearly 20 years, and invoking her doesn't necessarily win support today. The Tories' tough talk has coincided with the erosion of their lead as voters worry about losing benefits and public sector jobs. And while the blue-blooded Cameron sports a man-of-the people air, his inner circle has been less successful at showing sympathy for ordinary folk. Although few doubt that a renewed Brown premiership would be austere, voters may reckon it would be kinder than a Tory regime. "Bizarrely, with Labour all over the place [with their message], they are being consistent about protecting the safety net of public services," says Ben Page, chief executive of pollster Ipsos Mori.

Signs of economic improvement are also helping Brown. Home prices were actually up over the past year, and business confidence surveys are looking better. Andrew Hawkins, executive chairman of pollster ComRes, sees Labour gaining as "they get credit for the claim that they put in place the right measures to get out of the recession."

37%

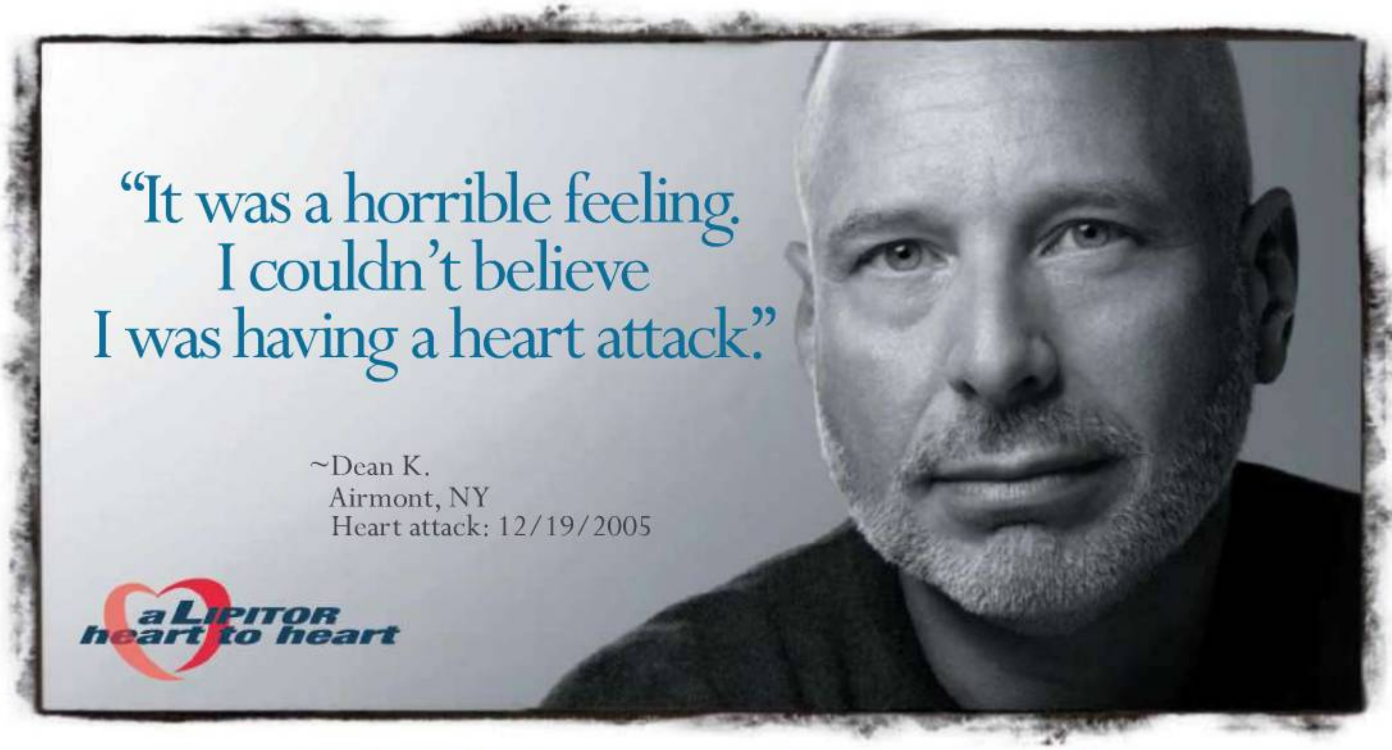
Voter support for Britain's Conservative Party, down from 48% in August 2008

Data: YouGov

With just about two months left before the expected election date of May 6, the outcome is impossible to predict. A Tory majority, a minority Labour government, or a split Parliament with the third-party Liberal Democrats holding the swing votes are all viable scenarios. The markets have a jittery season ahead of them. |BW|

DAN KITWOOD/GETTY IMAGES

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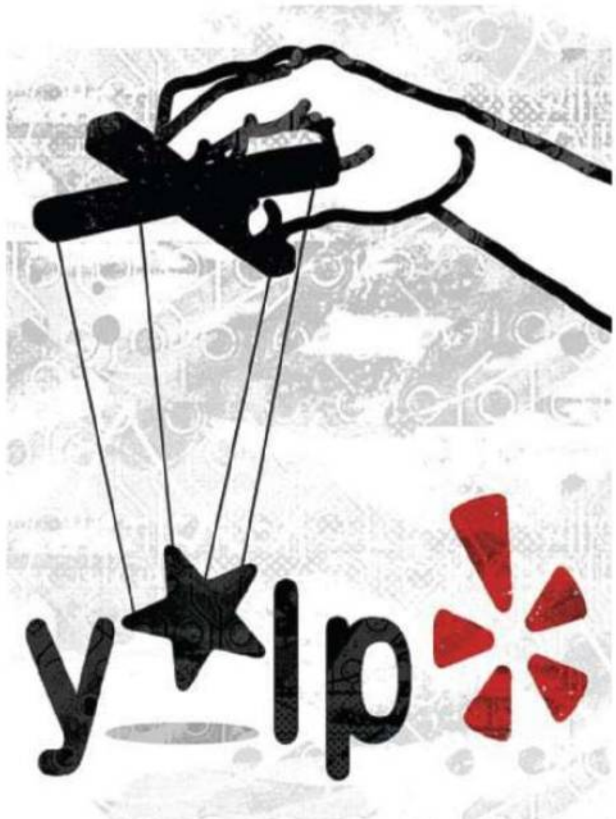
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Yelp: Advertise Or Else?

The site faces a lawsuit—and a barrage of criticism—for mingling ads and reviews

By Peter Burrows and Joseph Galante

Getting Yelped. That's the term angry business owners have started using when they feel unfairly criticized on the popular review site. Now Yelp is being forced to deal with its own unanticipated criticism. In a federal lawsuit filed in California on behalf of Long Beach's Cats & Dogs Animal Hospital, attorney Jared Beck claims that Yelp routinely highlights negative customer reviews unless business owners agree to advertise with the company. Beck, a Harvard-trained trial lawyer in Miami, says dozens of businesses have contacted him with similar allegations, and he plans to file an amended complaint with more companies in the coming weeks. "This is not an isolated incident," says Beck. "This seems to be a companywide practice."



Yelp co-founder Jeremy Stoppelman was dismissive of Beck's case in a blog post—"Lady Justice needs a lawsuit filter," he wrote. In his first extended interview on the issue, Stoppelman rejects the allegations and compares the suit to the criticism Google and eBay faced during their early years, when people were suspicious of ranking systems they didn't understand. "New technologies and business models can be confusing, and inevitably you have conspiracy theories," says Stoppelman, 32. "You have to take your blows."

Yelp's revenue comes from restaurants, hotels, and other businesses that typically pay $300 a month to advertise on the site, which 25 million people visit each month, according to research service Compete. It's a promising model—Elevation Partners agreed in January to invest as much as $100 million in the company—but because the subjects of Yelp's content (local businesses) are also its primary source of advertising, the potential for conflict is significant. "I'm not going to give Yelp any money," says Marianna Burmenko, the owner of Mara's Salon in San Francisco, who says the company is essentially asking for "bribes." Barry Hyde, who owns M&M Auto Werkes in Campbell, Calif., claims Yelp has repeatedly taken down positive reviews of his business because he refused to advertise. He's considering joining Beck's suit. "Let's put it this way: I run an ethical business," says Hyde, "and they don't." Stoppelman says Yelp never manipulates reviews to favor advertisers.

"LET'S PUT IT THIS WAY: I RUN AN ETHICAL BUSINESS, AND THEY DON'T"

Yelp has given companies the ability to respond publicly to critics on its site and provides tutorials to educate companies that may doubt the integrity of its rankings. Stoppelman says the company has also held meetings in five cities with more than 100 businesses and, over the next 90 days, executives will meet with groups such as the National Restaurant Assn.

Many analysts say it would help if the talk resulted in greater clarity. Currently, a restaurant owner can pay to have his favorite review appear at the top of a list of reviews, with only light shading and a small "sponsored result" label to differentiate it. Yelp may have to shift such advertising to one side of its Web pages to clearly delineate it from general reviews, says Danny Sullivan, editor of the Web site Search Engine Land. He also thinks Yelp should go further and let businesses opt out of having reviews altogether, an idea Stoppelman rejects out of hand.

Beyond the fate of Yelp, Beck's suit and the surrounding debate may help set new standards for reviews on the Internet. Joe Alexander, general manager of mattress maker Keesta International in San Francisco, calls Yelp "a phenomenal marketing tool for us," but says it has a "Wild West" atmosphere where many businesses try to manipulate reviews to their advantage. Stoppelman has to show he can lay down the law—or risk his company's future. |BW|

ILLUSTRATION BY GARY NEILL

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Condos for sale: Athletes stayed in the Millennium Water units

DARRYL DYCK/THE CANADIAN PRESS/AP PHOTO

Recovering from An Olympic Hangover

Vancouver put up $665 million so the Games could go on. Now it hopes the afterglow will help settle the debt

By **Christopher Donville and Chris Fournier**

With his overtime goal in the Olympic gold medal hockey match, Canada's Sidney Crosby set off a national celebration. Now the question is, can he move some luxury condos?

The party that lifted Canada's spirits also left Vancouver with a debt hangover, most of it in the form of $665 million the city borrowed and extended to the developer of the Millennium Water condominium complex where the Olympic athletes were housed. The city put up that money when financing fell through and now needs to sell the 474 remaining units in the complex, in a former warehouse district on the shores of False Creek, at prices that are expected to range from $580,000 to $9.6 million each. That would recoup the city's investment—raised by selling debentures and commercial paper, and tapping a credit line arranged by Toronto-Dominion Bank—and avert a cut to its credit rating. Vancouver officials hope the link to celebrity athletes such as Crosby will help juice sales. "The exposure of the Olympics has been the best possible marketing campaign," Mayor Gregor Robertson said just before the close of the Games. "We have a very good chance to see the village sold out within about two years."

Robertson and his team want to avoid a repeat of Canada's last Olympic-financing fiasco. The 1976 Summer Games in Montreal left Québec with $1.4 billion of debt that took three decades to repay. Vancouver's costs may rise depending on how long it takes to sell the units and recover the investment, officials say. The city of 600,000 was forced to step in after New York-based Fortress Investment Group withdrew support in late 2008 when it lost confidence in the developer, Millennium Development, amid cost overruns and the downturn.

$9.6 million

Priciest condos in the former Olympic Village

Data: Rennie Marketing Systems

As post-Olympics headaches go, this one is relatively mild. The Games, summer and winter, almost never cover their public costs. Vanoc, the local Olympics organizing committee, remains confident the final tab will fit within the $1.7 billion operating budget. But that doesn't include the province of British Columbia's share of subsidies, such as $579 million to upgrade the Sea-to-Sky highway between Vancouver and Whistler, B.C., where skiers competed, and nearly $2 billion to build a transit line between Vancouver's airport and downtown.

The picture isn't unremittingly bleak. Canada's gross domestic product grew by 5% in the fourth quarter and consumers are spending again, though unemployment remains high at 8.3%. As exports pick up, Vancouver—Canada's largest port—should benefit.

While the area's real estate values have rebounded from last year's lows, not everyone thinks the remaining condo units will cover the city's costs. Cameron McNeill, president of MAC Marketing Solutions, a Vancouver-based condo marketer, said units may need to sell for an average of $1,062 per square foot—steep even for a town with some of Canada's priciest properties. "It's kind of like having a car lot full of Ferraris," said McNeill, who represents a nearby rival development. "It's not like the car is bad. But there's a limited market for Ferraris and Lamborghinis."

The debt market remains wary. "Until they start selling these units, the risks will remain," says Alex Bellefleur, an analyst at Moody's, which has a negative outlook on the city's debt. Officials are counting on the afterglow of Canada's 14 gold medals to help clear the bill. Says Bob Rennie, whose Rennie Marketing Systems leads the sales effort: "In a perfect world, we'd love to have the athletes' signatures beside each front door." |BW|

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In Defense of Goldman. Really

Loopholes in EU rules, not Goldman Sachs, are to blame for Europe's debt troubles

COMMENTARY

By Mark Gilbert

This time, the vampire squid is innocent. The European Union is investigating Goldman Sachs Group's role in the financial maneuvering that helped Greece use swaps to postpone the day of economic reckoning past its ascension to euro zone membership. Goldman says, rightly, there was "nothing inappropriate" in the transactions it facilitated.

Most of the elements of a crime are present. There's a victim—trust in the common-currency project. There's a weapon, in the form of the derivatives that trimmed 2.37 billion euros ($3.2 billion) off the nation's debt burden. And there's a perpetrator, the Greek government, which knew its finances were too shaky to ditch its currency, the drachma.

There also seems to be an accomplice—Goldman Sachs, which had the financial engineering skills to crack open Greece's budget deficit and postpone enough of the country's obligations so it would qualify for entry into the euro zone. What's missing is any broken law. The architects of European integration knowingly and with malice aforethought added the words "additional measures" in a footnote to the blueprint. Those two little words were an acknowledgment that Italy would need to fudge its numbers to get into the club, giving the nation explicit permission to do whatever it took to massage the accounts into acceptable shape. They created a loophole that Greece was also able to exploit, in line with the rules, aided and abetted by Goldman Sachs.

So while German Chancellor Angela Merkel said last month "it's a scandal if it turned out that the same banks that brought us to the brink of the abyss helped fake the statistics," she's wagging her finger at the wrong party.

The DNA of investment bankers drives them to find and exploit malleable clauses, bend rules, take maximum advantage of the unintended consequences of legislation. Society doesn't want to outlaw investment banking (not yet, anyway). And creative accounting—which is just a polite way to talk about cooking the books—is nothing new for countries. Italy used a yen-denominated swap to give its finances a one-time puff and avoid the ignominy of failing to qualify for the euro. In the U.K., so-called public-private partnerships and private finance initiatives allow the government to shift the burden of costly infrastructure onto the balance sheets of companies that tender successfully to manage and build the projects. The companies get access to rampant profit potential in return for the government's suppressing its own debt burden.


The Greek finance chief unveils budget cuts

As for Greece, recall that in September 2004 the nation had to revise upward its deficits for 2000, 2001, and 2002. It turned out that the country had missed the 3% deficit threshold for euro zone membership in every single year since it joined the common currency—transgressions that went unpunished. So no one should be surprised that Greek Finance Minister George Papaconstantinou confessed to "some sleight of hand" in Greece's 2009 deficit numbers.

The Greece debacle is likely to hasten increased oversight of the derivatives market. In particular, contracts where the buyer doesn't have any skin in the game are akin to writing auto insurance for people who don't own a car and don't even have a driver's license, but who nevertheless fancy a bet on the likelihood of a car crash.

Financial authorities will probably outlaw such behavior, ignoring the difficulties of differentiating between efficient risk management and risk creation.

LIGHTNING ROD

Moreover, governments are clearly uncomfortable with the concept of investors being able to bet against a country's creditworthiness in the credit-default swaps market. This may spur an unwelcome round of regulation. The trick Goldman employed to help Greece massage its debt figures hinged on using historical, rather than prevailing, currency rates in a series of swap transactions.

While that undoubtedly comes under the heading of fast-and-loose, it's not illegal; swaps are over-the-counter contracts between consenting adults, so no matter how divorced the values are from reality, it really isn't anybody else's business.

Goldman has become the lightning rod for public anger about the bailout of the finance industry. The vexation is appropriate; the bankers fail to see that every financial firm would be dead without an ocean of taxpayers' money keeping the system afloat. In the case of Greece's swaps, though, Goldman Sachs has done nothing wrong. The EU's forensics squad should be looking closer to home for its culprit. |BW|

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Lessons of a $618,616 Death

BY AMANDA BENNETT

IT WAS SOMETIME AFTER MIDNIGHT ON DEC. 8, 2007, when Dr. Eric Goren told me my husband might not live till morning. The kidney cancer that had metastasized almost six years earlier was growing in his lungs. He was in intensive care at the Hospital of the University of Pennsylvania in Philadelphia and had begun to spit blood.

Terence Bryan Foley, 67 years old, my husband of 20 years, father of our two teenagers, a Chinese historian who earned his PhD in his sixties, a man who played more than 15 musical instruments and spoke six languages, a San Francisco cable car conductor and sports photographer, an expert on dairy cattle and swine nutrition, film noir, and Dixieland jazz, was confused. He knew his name, but not the year. He wanted a Coke.

Should Terence begin to hemorrhage, the doctor asked, what should he do?

This was our third end-of-life warning in seven years. We had fought off the others, so perhaps we could dodge this one, too. Terence's oncologist and I both believed that a new medicine he had just begun taking, Pfizer's Sutent, would buy him more life.

Keep him alive if you can, I said.

Terence died six days later, on Friday, Dec. 14.

What I couldn't know then was that the thinking behind my request—along with hundreds of decisions we made over the years—was a window on the impossible calculus at the core of today's health-care dilemma. Terence and I were eager to beat his cancer. Backed by robust medical

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AS COSTLY AS HIS TREATMENT WAS, no one can

insurance provided by a succession of my corporate employers, we were able to wage a fierce battle. As we made our way through a series of expensive last chances, like the one I asked for that night, we didn't have to think about money, allocation of medical resources, the struggles of roughly 46 million uninsured Americans, or the impact on corporate bottom lines.

Terence's treatment was expensive. The bills for his seven years of medical care totaled $618,616, almost two-thirds of which was for his final 24 months. Still, no one can say for sure if the treatments helped extend his life.

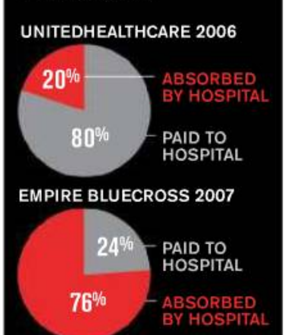
Over the final four days before hospice—two in intensive care, two in a cancer ward—our insurance was billed $43,711 for doctors, medicines, monitors, X-rays, and scans. Two years later the only thing I can see that the money bought for certain was confirmation he was dying. Along with a colleague, Charles Babcock, I spent months poring over almost 5,000 pages of documents collected from six hospitals, four insurers, Medicare, three oncologists, and a surgeon. Those papers tell the story of a system filled with people doing their best. Stepping back and looking at that large stack through a different lens, a string of complex questions emerges.

31% FOR PAPERWORK

Health-care costs represent 17% of today's U.S. gross domestic product. Medicare devotes about a quarter of its budget to care in the last year of life, according to the policy journal *Health Affairs*. Yet as I fought to buy my husband more time, it didn't matter to me that the hospital charged more than 12 times what Medicare then reimbursed for a chest scan. It also didn't matter that UnitedHealthcare reimbursed the hospital for 80% of the $3,232 price of a scan, while a few months later our new insurer, Empire BlueCross & BlueShield, paid 24% for the same test. And I didn't have time to be thankful that the insurers negotiated the rates with the hospital so neither my employers nor I actually paid the difference between the sticker and discounted prices.

Looking at that stack of documents, it is easy to see why 31% of the money spent on health care went to paperwork and administration, according to research published in 2003 in the *New England Journal of Medicine*. That number has stayed the same or grown since then, says Dr. Steffie Woolhandler, a professor at Harvard Medical School and a co-author of the study. Often Terence's bills, with their blizzard of codes, took days to decipher. What did "opd patins t"

The bill for a chest CT scan at the Hospital of the University of Pennsylvania was $3,232. Here is the amount as covered by two insurers:



PHOTOGRAPH BY ANDREW HARRER/BLOOMBERG; CHARTS BY STANFORD KAY

WHO PAID FOR TERENCE'S TREATMENT?

A collection of documents shows the breakdown



$618,616

Total billed for medical care over seven years. Two-thirds of that was for the final 24 months.

$254,176

Total paid by insurers after they imposed discounts.

$9,468

Total paid by family.

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say for sure if it helped to extend Terence's life



4,750

Approximate number of pages of medical records collected from Medicare, six hospitals, four insurers, three oncologists, and a surgeon.

Data: Terence Foley's medical and insurance records

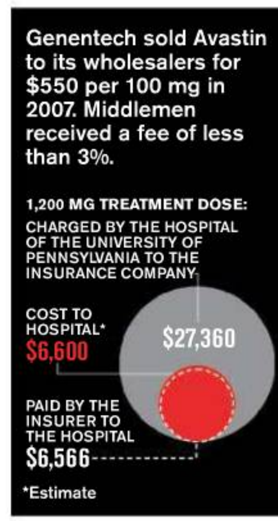
or "bal xfr ded" mean? Was the dose charged the same as the dose prescribed?

The documents revealed an economic system in which the sellers don't set the prices and the buyers don't know what they are. Prices bear little relation to demand or how well goods and services work. "No other nation would allow a health system to be run the way we do it. It's completely insane," said Uwe E. Reinhardt, a political economy professor at Princeton University who has advised Congress, the Veteran's Administration, and other federal agencies on health-care economics.

In reviewing Terence's records, we found Presbyterian Medical Center in Philadelphia charged UnitedHealthcare $8,120 in 2006 for a 350 mg dose of the drug Avastin, which should have been free as part of a clinical trial. When my Bloomberg colleague inquired, the 80% insurance payment was refunded. A small mixup, but telling.

Some drugs Terence took probably did him no good. At least one helped fewer than 10% of patients. Today, pharmaceutical companies and government agencies are trying to sort out the economics of developing drugs that will help only a small subset of patients. These drugs are very expensive. Should every patient have the right to them?

Terence and I answered yes. Each drug potentially added life. Yet that, too, led me to a question I still can't answer. When is it time to quit? Congress dodged the question last year as it tried to craft a health-care bill. The mere hint of limiting the ability to choose care created a whirlwind of accusations of "death panels."



One thing I know is that I don't envy the policymakers. As the health-care debate heated up, I remembered the fat sheaf of insurance statements that had piled up after Terence's death. Our children, Terry, 21, and Georgia, 15, assented to my idea of gathering every record to examine what they would show about end-of-life care—its science, emotions, and costs. Terence would have approved.

Taking it all into account, the data showed we had made a bargain that hardly any economist looking solely at the numbers would say made sense.

Why did we do it? I was one big reason. Not me alone, of course. The system has a strong bias toward action. My husband, too, was unusual, said Keith Flaherty, his oncologist, in his passionate willingness to endure discomfort for a chance to see his daughter grow from a child to a young woman, and his son graduate from high school.

After Terence died, Flaherty drew me a picture of a bell

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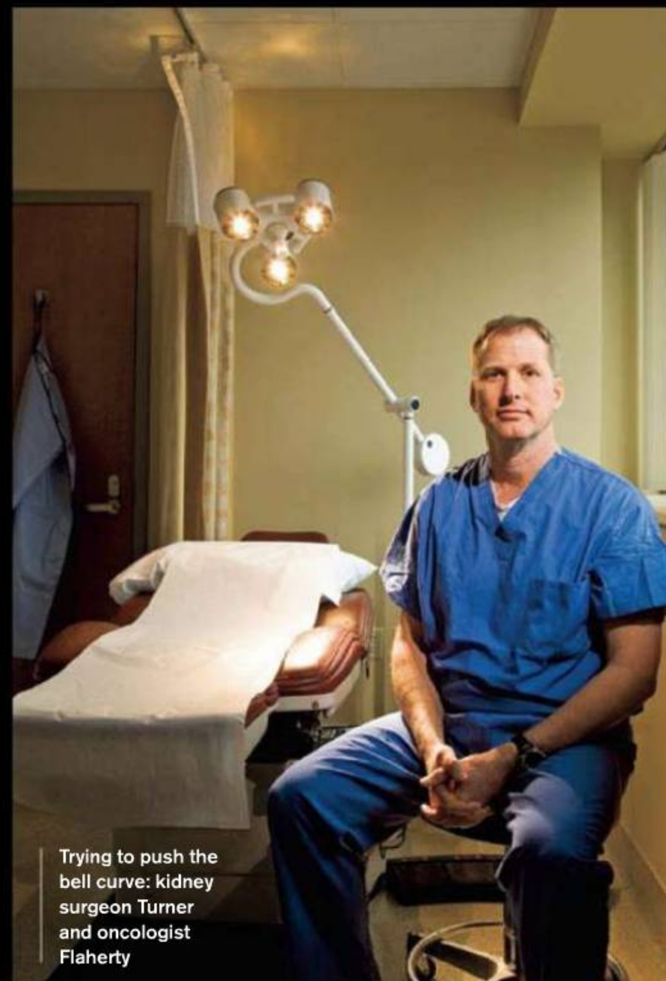
AN EXPLOSION OF DRUG DISCOVERIES had made

curve, showing the range of survival times for people with kidney cancer. Terence was way off in the tail on the right-hand side, an indication he had beaten the odds. For many, an explosion of research and drug discoveries had made it possible to daisy-chain treatments and extend lives for years—enough time to keep our quest from having been total madness.

Terence used to tell a story, almost certainly apocryphal, about his Uncle Bob. Climbing aboard a landing craft before the invasion of Normandy, Bob's sergeant was said to have told the men that by the end of the day, 9 out of 10 of them would be dead. Said Bob: "Each one of us looked around and felt so sorry for those other nine poor sonsabitches."

For me, it was about pushing the bell curve. Knowing there was something to be done, we couldn't not do it. Believing beyond logic that we were going to escape the fate of those other poor sonsabitches.

It is hard to put a price on that kind of hope.



Trying to push the bell curve: kidney surgeon Turner and oncologist Flaherty

(L TO R) ROBBIE MCCLARAN; DANA SMITH

A SHADOW, BUT GOOD ODDS

We found the cancer by accident, on Sunday, Nov. 5, 2000, in Portland, Ore. Terry had invited a dozen friends for a sleepover to celebrate his 12th birthday. I was making pancakes and shipping the boys home. Terence had been having stomach cramps for weeks. Suddenly he was lying on the bed, doubled over in pain. Our family doctor ordered him to the emergency room.

We were immediately triaged through. Not a good sign, I thought. The kids sat on the waiting-room floor, Barbies and X-Men around them, while Terence writhed in a curtained alcove. When he returned from a scan, the doctor said, almost as an aside: There's a shadow on his kidney. When he's feeling better, you should take a look at it. Both of us were annoyed. Why would we think about a shadow on his kidney? That wasn't the problem. He was in such pain he could barely breathe.

The cause of the pain turned out to be violent ulcerative colitis. The damaged colon was removed on Dec. 13, in an operation that left Terence so weak that he spent three weeks, including Christmas morning, immobile in a chair. Colleagues delivered meals to the house. My sister wrapped presents. My boss sent over her husband to put up our lights. I felt so bad for Terence that I got him a cat, the pet he had long wanted. The orange kitten howled in a box under the tree.

And the shadow? We were so grateful he was out of pain that we would have ignored it had someone from the hospital not called to urge us to find out what it meant. Within a month, Terence was in surgery again. On Jan. 18, Dr. Craig Turner removed the diseased kidney. Emerging from the five-hour operation, Turner confirmed the worst: He believed the shadow was cancer. A week later, when Terence was well enough to walk into the doctor's office, Turner was reassuring.

"We got it all," he said.

Terence teared up. "Thank you for saving my life."

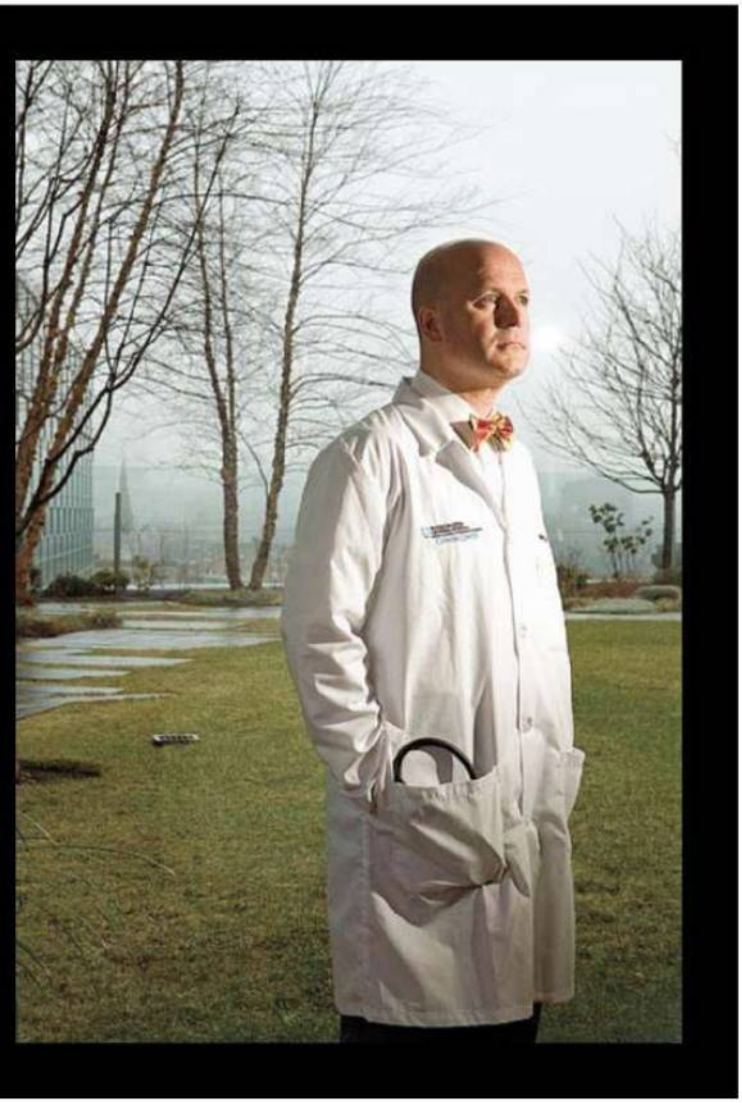
The bills from Regence BlueCross BlueShield of Oregon show the operation was relatively inexpensive, just over $25,000, about 4% of the eventual total charged to keep Terence alive. Our share was $209.87. I never looked at or thought about the total cost, or the $14,084 that our insurance—in reality, my employer—paid. We never had to consider who was actually shouldering the bills.

Kidney cancer is uncommon, accounting for about 3% of all cancers, or about 50,000 new cases in the U.S. last year, according to the Kidney Cancer Assn. Terence was a typical patient: an older man, overweight, and an ex-smoker. Asymptomatic for a long time, most kidney cancers are discovered accidentally or too late. So we felt lucky. The first tool for fighting kidney cancer is usually the one used since medieval times: the knife, or its technological equivalent. If a tumor is removed early enough, before it flings microscopic cells into the bloodstream that can implant in other organs, surgery is close to a cure.

For Terence the odds looked good. His 7-centimeter tumor

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daisy-chain treatments possible, buying time



showed no signs of having spread. According to the traditional method of evaluating, or staging, the cancer, that meant he had an 85% chance of surviving five years. A lab report soon chilled our optimism. Tests on Terence's tumor showed that he had so-called collecting duct cancer. Named for the part of the kidney where it is thought to originate, collecting duct is the rarest and most aggressive form of kidney cancer. In my online research, almost everyone who had it died within months, sometimes weeks, of diagnosis.

Most kidney cancers don't respond well to chemotherapy. There was no accepted treatment after surgery. Almost nothing was known about collecting duct cancer. Only about 1% of kidney cancer patients receive that diagnosis. Dr. Turner and I could find just 50 cases documented in the medical literature worldwide, and nothing had proved effective in halting it. "Watchful waiting" was the recommended path.

Waiting for him to die was what we feared.

He didn't die. He got better. We didn't know why. We tried not to think about it.

By the spring of 2002, we had moved to Lexington, Ky., where I was the editor of the local newspaper and Terence was creating an Asia Center at the University of Kentucky. He seemed fine. He began moving Chinese and Japanese history books to his office. On Saturdays we drove through the bluegrass to take seven-year-old Georgia to riding lessons. We reluctantly let 13-year-old Terry crowd-surf at his first rock concert.

Then, on May 6, 2002, Terry called me at work, panic in his voice. "Mom, come home. Dad is very sick."

His father was in bed, his face flaming with fever, shaking with chills under a pile of blankets. He could barely speak. "The cancer is in my lungs," he said. "I've got six to nine months left."

FEAR, AND AN INTERNET PLUNGE

He had been keeping that secret for months. In February, routine follow-up scans had spotted the cancer's spread. "The first thing Terence said was, 'Doc, do you have any female patients who have recently died? I need to find a widower so my wife can meet her next husband,' " his Lexington oncologist, Dr. Scott Pierce, later recalled. After more tests, Dr. Pierce prescribed Interleukin-2 because there were no other options. Injections of the protein, at $735 a dose, were intended to stimulate the immune response to help fight the cancer's invasion. The overall response rate was only about 10%. For most patients, Interleukin-2 did absolutely nothing.

Terence hadn't wanted to worry us. In his mind, if he recovered, we would never know how close he came; if he died, he would have spared us months of anguish. He started a diary and spent more time in the office so we would get used to his absence.

His secret was betrayed by his violent reaction to his first dose of IL-2. Suddenly his actions over the last several weeks made sense. He had been giving away musical instruments and pieces of art. "I have too much stuff," he had told me, a bizarrely improbable statement coming from him. I was amused, exasperated, and touched by his desire to protect us. Even under the strain of his disease, he was so much himself. "Did you think I wouldn't have noticed if you didn't come home one day?" I asked.

I spent that night awake in our dark living room. For the first and only time, I felt pure terror. A few days later I visited a therapist.

"I can't survive without him," I said.

"What does he say when you feel this way?" she asked.

"He says I can handle anything."

"You'll need to say that to yourself."

Terence stopped taking IL-2 after a few weeks of treatments, unable to stand the side effects.

I plunged into the Internet. If there were something out

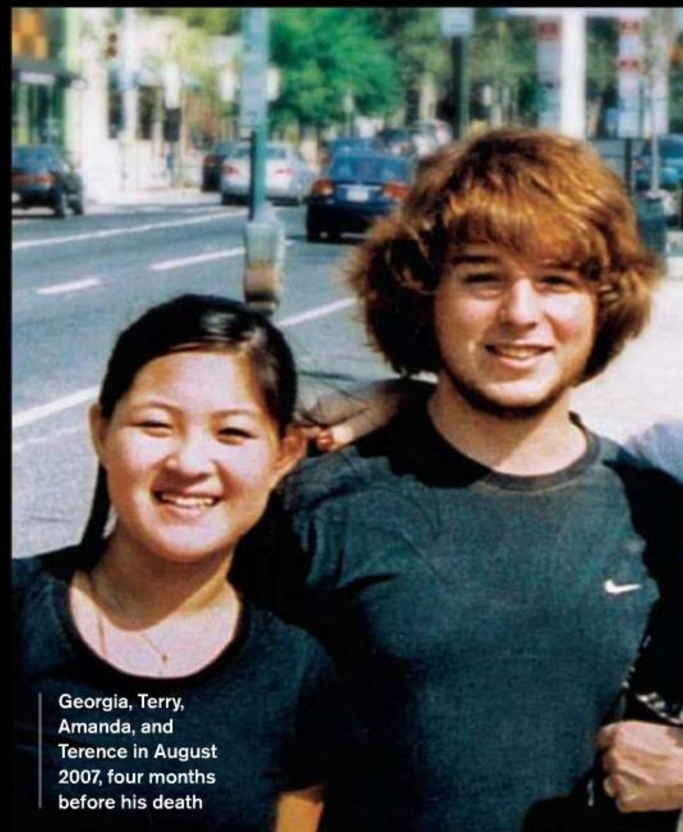
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THE PULMONOLOGIST mentioned it might be time

there that could save him, I was going to find it. Years before, one of my former colleagues, dying from AIDS, had suddenly come back to vigorous life because of a chance introduction to a doctor who prescribed what was then an experimental antiviral cocktail. Another had beaten leukemia with a cutting-edge bone marrow transplant. We could defeat this.

I downloaded papers, presentations to the Kidney Cancer Assn., abstracts from the National Library of Medicine. I called researchers and oncologists, pathologists and fellow journalists. When the research became overwhelming, I hired a retired nurse to help. My boss's wife, a nurse herself, dug in too. After I messaged one couple about a clinical trial in Texas, they offered us their spare bedroom.

Throughout the spring and summer of 2002, Georgia, then 8, rode her bicycle up and down shady South Ashland Avenue. Thirteen-year-old Terry and his friends Shannon, Hughes, and Tanner came in last at their first battle of the bands. Terence sounded optimistic. "It's my dream," he said. "Some day we're going to gig together."



Georgia, Terry, Amanda, and Terence in August 2007, four months before his death

AWAITING SCANS, LEARNING THE VIOLIN

The truth was we were both shaken by the dire prognosis.

"What would you regret dying without having seen?" I asked. He answered without hesitation: "Pompeii." We pulled Terry from his eighth-grade class, Georgia out of second, and flew to Italy to see the excavated remains of the city once buried under volcanic ash. We walked the cobbled streets, poked into frescoed houses, taverns, and baths, and took an eerie comfort from the 2,000-year-old shapes of families huddled together, trying to ward off disaster.

By then our research had led us to the Cleveland Clinic, where Dr. Ronald Bukowski had specialized in kidney cancer for over 20 years. At our first meeting, in August 2002, Terence explained that he had collecting duct cancer.

"No you don't," Bukowski said.

We were confused. How did he know?

"You're sitting here," he said. "If you had collecting duct, you would be dead."

Bukowski argued that the disease was growing so slowly that we should simply watch and wait. We did, for three years. Then, in December 2005, a scan showed that the cancer in his lungs had begun to grow.

By this time, research had progressed. New drugs designed to attack a tumor's blood supply were appearing to slow the growth of a wide range of cancers. Bukowski recommended we enter a clinical trial, pretty much the only way to get these targeted therapies. He referred us to Dr. Flaherty in Philadelphia, where we had moved in June 2003 when I changed jobs.

The drugs Flaherty was testing—Genentech's Avastin and Bayer's Nexavar—had showed promise individually. The trial would find out how they worked together. In March 2006, Terence took his first intravenous dose of Avastin, an hour-long process, and swallowed his first Nexavar. The side effects were hard. There were rashes, sometimes debilitating stomach pains. But he continued teaching, picking up the kids at school, studying and writing. He worked on his book, a grammar text based on classical Chinese poetry. He started to learn to play the violin and to read and write Arabic. Every two weeks he went for an Avastin drip. And every month we anxiously awaited the results of a chest scan.

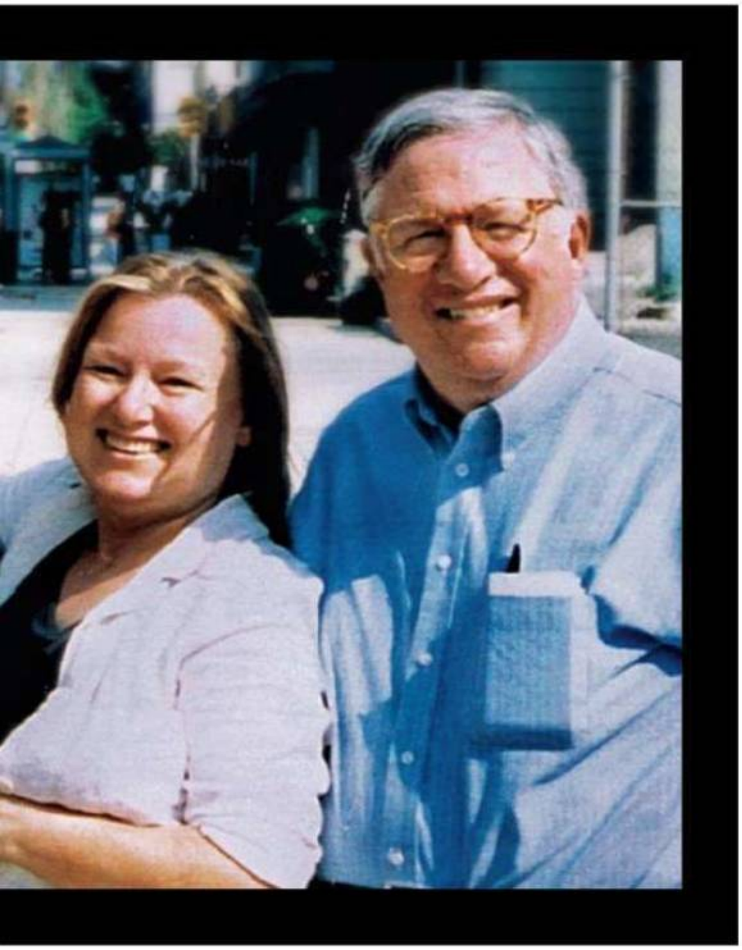
At first the cancer didn't budge. Then it began to retreat.

Because Terence was in a clinical trial, Genentech and Bayer provided their drugs free. I learned that over the years of Terence's battle with cancer, some insurers drove harder bargains than others. In December 2006, for example, United Healthcare paid $2,586 to University of Pennsylvania Hospital for a chest scan; in March 2007, after I switched employers, Empire BlueCross paid $776 for the same $3,232 bill.

When it came to the insurance companies, the sticker price meant little since they had negotiated their own deals with the hospital. Neither the hospital nor the insurance companies would elaborate. The entire medical bill for seven years, in fact, was steeply discounted. The $618,616 was lowered to $254,176 when the insurers paid their share and imposed their discounts. The portion of the charges that

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to consider hospice. We brushed off the suggestion



were not covered for the most part vaporized. Terence and I were responsible for and paid $9,468—less than 4%.

During the trial, Terence packed boxes for the troops in Iraq and Afghanistan, loading them in our kitchen with deodorant, wet wipes, Mars bars, Kool-Aid, beef jerky, batteries, and magazines. A veteran of Naval Intelligence and the U.S. Air Force reserves, he walked almost every day to the post office with a box addressed to "Any Soldier." Behind the counter, the smiling lady with the long red hair extensions became his friend, and every so often a soldier would drop him a thank-you note.

Life went on.

Then, in August 2007, from half a world away, I heard the cancer return.

I was on a business trip to China when Terence coughed during one of our phone calls. By the time I got home, scans had confirmed growth of one of the lung's cancerous spots.

By now, more than six years had passed since we first saw the shadow, and I was used to the scares. Avastin's side effects—fatigue, stomach ailments, rashes—had been getting him down, and the doctor had agreed back in May to let him stop treatments. So we'll go back on the Avastin, I thought, or cut out or laser out the growth, add new treatments, and go on.

The records document our renewed fight. Terence resumed Avastin. Because he was no longer in a trial, our insurance company was billed $27,360 a dose, every two weeks, more than the cost of the kidney surgery in 2000. Empire BlueCross paid $6,566.40. We paid nothing. So who did the paying? The health insurance system depends on healthy people bearing the cost for sick ones like Terence. For all its incredible treatment benefits, the system is untenable. Should you have had a voice in Terence's final days? Would I make the same decision with my money for your loved ones? These are things I think about now but can't answer.

NO CONSENSUS

He coughed almost continuously. His weight plunged. He needed help on the stairs. He began to use a cane. When his friend Woody came to visit, Terence couldn't muster the breath to blow his cornet. He coughed and coughed and coughed. In the last week of October, he called me at work.

"I can't pick Georgia up at school," he said. "I can't get out of the chair." On Halloween, his Dracula costume stayed in the basement. We left the candy on the doorstep.

On Nov. 8 we saw Dr. Ali Musani, a pulmonologist specializing in cancer. We hoped that the growing tumor in Terence's chest could be removed. Unable to stand or sit unassisted, he lay on the floor and refused to get up. Alarmed, Musani admitted him to the hospital. He said there was nothing he could do about the tumor. He gently mentioned that it might be time to consider hospice. We brushed off the suggestion.

Terence stayed in the hospital four days. Meanwhile a quiet tension was building. Flaherty and I believed this episode to be a temporary setback. Other doctors and nurses saw a patient near the end.

On Nov. 11, before discharging him, a doctor propped one of Terence's scans on a light board so we could clearly see the blizzard of white spots, hundreds of tumors, covering his lungs.

Avastin wasn't stopping them.

Flaherty was not fazed by the growth, and pointed out that many of the doctors looking at the scans didn't understand the course of kidney cancer. He and I wanted to move on to the next link in the daisy chain of newly available drugs. Sutent, another targeted therapy, had been approved the year before. It worked as Avastin did, by stopping cancer's ability to build extra blood vessels to feed its growth, but in a different way. One $200 pill a day. A shot at more life. Sutent might have more serious side effects—rashes, fatigue, stomach distress, strokes—but Terence was game. He began taking it on Nov. 15.

At home, he drew a line down the middle of a piece of paper. On one side he wrote things to throw away. On the other, things to keep.

"Stop that!" I snapped. "You aren't going to die."

I prepared for what I expected would be a new phase of our life. I found protein drinks online and protein bars in a bodybuilding shop. I got forms for a handicapped license plate,

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HOW DO YOU PUT A PRICE on 17 months?

looked into outfitting our row house with a stair lift.

Terence was no longer able to get in and out of bed alone, so I hired a health aide. Whatever he craved, I bought. I wrote down everything he ate. Cold grapefruit slices. Chicken noodle soup. Clam chowder. I counted the calories he consumed one day: 210.

On Friday, Dec. 7, just as the aide was packing to leave for the day, Terence looked up, startled, as the corners of his mouth foamed bright red with blood. It was a struggle to get him down our narrow stairs to the ambulance. In the emergency room it was clear something was seriously wrong. "What's your name?" asked the ER doctor. Terence responded correctly. "What's the date?" Terence gave the doctor what the kids and I recognized as "Daddy's 'Just how dumb are you?'" look. But he couldn't answer.

"Who's the President of the United States?" That triggered something. "That moron, Bush," he said.

Terence was admitted that night to a ward where Eric Goren was doing his last intensive-care overnight shift of a three-year residency. In a small break room, alongside vending machines selling soft drinks and chips, Goren told me that bleeding from the lungs might suddenly become uncontrollable. If that happened, what should he and his team do?

I wanted to see whether Flaherty still believed Sutent could make a difference, but I couldn't reach him. Goren and I settled on what the hospital called Code-A. Do everything possible to prevent a major bleed or anything life-threatening. But don't take heroic measures if death seems inevitable.

I called the children to the hospital.

My decision about Terence's treatment, so hard on Saturday, was easy by Monday. The scans now were showing signs of cancer in his brain, surrounded by a cascade of hundreds of tiny strokes. I had Terence's signed living will, but I didn't need it. I knew what this man who lived for books, music, and ideas would want.

When Flaherty arrived, he looked shaken. "I didn't expect this," he said.

That afternoon I signed the papers transferring Terence to hospice. The next day the hospital staff took away the machines and the monitors. The oncologists and radiologists and lab technicians disappeared. Hospice nurses, social workers, chaplains, and counselors for me and the children—began to arrive and the focus shifted from treatment to easing our transition.

Over the next three days we were charged $14,022 for the same hospital bed. Included were the pain and anxiety medications Ativan and Dialaudid, his monitoring, and counseling for a different kind of pain management for me and the children. The bill was less than a third of the previous four days' $43,711.

Terence drifted into a coma on Tuesday. I e-mailed his friends and read their goodbyes aloud, hoping he could hear and understand. I slept in a chair. At about 2:30 a.m. Friday, a noise in the hall startled me. I awoke just in time to hold his hand as he died.

They gave me back his wedding ring the next day.

Ten days later, the kids hung Daddy's Christmas stocking alongside our three. I mailed the cards he had addressed months earlier, slipping in a black-bordered note. I threw away the protein bars, gave the energy drinks to a shelter, and flushed an opened bottle of Sutent down the drain.

Looking back, memories of my zeal to treat are tinged with sadness. Should I have given up earlier? Would earlier hospice care been kinder? I hadn't believed Terence was going to die so I had never confronted any of those dilemmas. And I never let us have the chance to say goodbye.

I think had he known the costs, Terence would have objected to spending an amount equivalent to the cost of vaccine for nearly a quarter million children in developing countries. That's how he would have thought about it.

But when I ask myself whether I would do it all again, the answer is—absolutely. I couldn't not do it again.

SECOND-GUESSING

Late last year, I waded through a snowstorm to Keith Flaherty's office in Boston, where he had moved to a new job. Did we help Terence or harm him? There's a possibility, he said, that the treatment actually made the cancer worse, causing it to rage out of control at the end. Or, as another doctor suggested in passing at the time, the strokes were a side effect of the Sutent and not the cancer.

But neither Flaherty nor I believe that. The average patient on Flaherty's trial got 14 months of extra life. Without any treatment at all, Flaherty estimates that for someone with Terence's stage of the disease it was three months. Terence got 17 months—still within the realm of chance but on the far-right side of the bell curve.

There is another bell curve that Terence did not live to climb. It charts the survival times for patients treated not just with Sutent, Avastin, and Nexavar, but also Novartis' Afinitor and GlaxoSmithKline's Votrient—both made available since Terence's death. Doctors and patients now are doing what we dreamed of, staggering one drug after another and buying years more of life.

Slides on the results of Flaherty's clinical trial, presented at the 2008 meeting of the American Society of Clinical Oncology, showed that Avastin and Nexavar worked well on a wide variety of patients. Only Flaherty and I know that the solitary tick mark at 17 months was Terence.



Only I know that those months included an afternoon looking down at the Mediterranean with Georgia from a sunny balcony in southern Spain. Moving Terry into his college dorm. Celebrating our 20th anniversary with a carriage ride through Philadelphia's cobbled streets. A final Thanksgiving game of charades with cousins Margo and Glenn.

And one last chance for Terence to pave the way for all those other poor sonsabitches. |BW|

–With Charles Babcock

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[1] Financial Times, July 19 2009, Title: How to End America's Deadly Coal Addiction by: Robert F. Kennedy Jr.

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THE OTHER RON BURKLE

THE BILLIONAIRE HAS BEEN BELITTLED FOR HIS CELEBRITY FRIENDS AND BITTER LAWSUITS. BUT HIS MOVES ON BARNES & NOBLE AND BARNEYS ARE NO LAUGHING MATTER

By Susan Berfield
Photograph by Brad Trent

If you've come across the name Ron Burkle, you probably know that he's a billionaire. That's because Burkle's wealth is usually deployed as an adjective and almost always with a hint of derision. As in, Ron Burkle, billionaire playboy. Or Ron Burkle, billionaire friend of Bill Clinton.

Adjectives are hard to shake, which is why it's often overlooked that Burkle—billionaire playboy friend of Bill Clinton—is also a shrewd and secretive investor and, to the surprise of many, self-made. A former stock boy who got rich buying and selling grocery stores, Burkle, 57, owns almost 30% of A&P and has a major say in its management. He's worth $3.2 billion, according to *Forbes*. Now he wants control of Barneys, the troubled style supermarket of the rich, and to enlarge his holdings in Barnes & Noble, a company that Burkle thinks he can save from becoming the Tower Records of the book business.

Burkle's overtures have met with hostility. Barneys is publicly ignoring him. Barnes & Noble's founder and chairman, Leonard Riggio, changed the bylaws to keep him from gaining shares and influence. Both companies appear to be hoping he'll get frustrated and go away. "Ron doesn't take no for an answer," says Lloyd Greif, who runs the investment banking firm Greif & Co. in Los Angeles and has known Burkle for decades. "I think people should be mindful of who they are dealing with." Frank Biondi, the former Universal Studios chief who advised Burkle on a possible purchase of Tribune Co. in 2007, adds: "When Ron gets pushback, he pushes back harder."

Burkle hasn't granted an interview in three years. He agreed to speak with *Bloomberg BusinessWeek* because he's feeling good about the past year and, in light of his dustups with Barneys and Barnes & Noble, wants to give his side. At the La Jolla (Calif.) mansion he uses as a business retreat, Burkle pads around in his favorite outfit: short-sleeve black Ralph Lauren polo shirt, cargo pants, and well-worn sneakers. He doesn't offer a tour or much by way of introduction. It's his world, his rules.

FROM STOCK BOY TO F.O.B.

Burkle's firm, Yucaipa Cos., controls some $9 billion, and he prefers to put much of that into private companies, where he can hold sway unobserved. (Yucaipa's biggest investment, roughly half a billion dollars, is in AmeriCold Logistics, a realty trust and owner of temperature-controlled warehouses.) Explaining his philosophy, Burkle says: "We always try to buy companies that are doing O.K. but that have some issues. We buy at a price that if they just muddle through, we don't go broke. And if they do better, we make a lot. Since I was 13, I've been buying things because they are ridiculously cheap. I tell my people, 'Don't explain what we're doing. They'll think we're geniuses if they don't know.'"

At 13, Burkle earned his trading money by working as a box boy at a Stater Brothers grocery store in Pomona, Calif. His father, now in his 80s, managed another store in the chain. After Burkle dropped out of nearby California State Polytechnic University, he returned to Stater, moved up the management

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Burkle at his New York home: "Since I was 13, I've been buying things because they are ridiculously cheap"

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RON'S WORLD

Burkle has enjoyed a wide circle of famous friends. His increasing number of high-profile investments has gotten less attention.

THE POLITICIANS

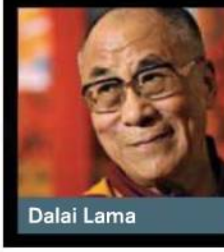


Bill Clinton



Al Gore

THE HOLY MAN



Dalai Lama

THE CELEBRITIES



Leonardo DiCaprio

ranks, and assembled a group of investors to make a bid when the parent company decided to sell the chain in 1982. The board rejected it as too low and fired him. "I felt pretty horrible," he recalls. "My dad had worked there almost his whole life. It was the only place I had ever worked. I thought it was a once in a lifetime opportunity to own a company, and I'd missed it."

The regret didn't last long. Burkle, who had made money investing in currencies and commodities, bought and flipped a few small grocery stores—at least one with junk-bond financing from Michael Milken—and in the process realized he had found his calling. He formed Yucaipa, named after the small southern California town where he was living, in 1986. He says Yucaipa has completed some 40 mergers and acquisitions worth $30 billion in the years since. (His biggest coup came in 1998, when he sold the Fred Meyer chain to Kroger in a deal valued at $13.5 billion.) Yucaipa reports that its funds have an average annual return of 40%, a figure that, because of the minimal reporting required of private equity firms, is impossible to verify.

Around 1990, Burkle, a social liberal and fiscal conservative, started holding political fund-raisers at his Green Acres estate in Beverly Hills. That drew notice from then Arkansas Governor Bill Clinton. They met for the first time at Green Acres in 1992, and the two ambitious men from modest beginnings became fast and close friends. Since 1992, Burkle has donated $1.86 million to the Democratic Party.

When President Clinton visited Los Angeles, he often stayed at Green Acres. For five years after Clinton left office, he was an adviser to Yucaipa, earning at least $15 million for making phone calls, brokering introductions, and giving speeches on Yucaipa's behalf. The relationship was meaningful and transactional. Clinton, who refused comment for this story, brought Burkle into circles of government and celebrity he would never have been able to crack on his own. Burkle gave Clinton high-paid, easy work. Each brought the other a fair amount of trouble. "When Clinton left the Presidency he had to make money, and there were certain limits on how he could do it," says Burkle. "In that regard, having him work for Yucaipa was the right thing to do. In other ways, it was the dumbest thing I ever did."

Clinton's post-Presidential business and social life received intense scrutiny, and Burkle—the divorced billionaire with a Boeing 757—became an object of curiosity and often scorn. "If someone wanted to embarrass [Clinton], I got thrown in it, too," says Burkle. "I got all that for free." Burkle also received a lot of attention when he unsuccessfully sued Michael Ovitz over a failed partnership and when he claimed he was the victim of an extortion attempt by a New York gossip reporter.

When Hillary Clinton was nominated as Secretary of State in 2008, Bill severed his ties with Yucaipa and Burkle. Some of Yucaipa's business dealings were getting messy. It hired as a consultant the now jailed Italian developer Raffaello Follieri and took on Sheikh Mohammed bin Rashid Al Maktoum, the ruler of Dubai, as a partner. Burkle says he and Clinton don't seen much of each other anymore and explains the rupture this way: "Before, every trip with him seemed like a once in a lifetime opportunity. Now I have so many things to do."

> **"BARNES & NOBLE IS IN CONTEMPT OF RON, AND THAT'S NOT A GOOD OFFENSE. ... MOST FOLKS LIVE TO REGRET THAT"**

RECESSION RICHES

The Great Recession held promise for an investor like Burkle. It was the stock prices in 2007 that signaled to him the economy was in trouble. They were so high that he felt compelled to sell, and there was nothing he considered cheap enough to buy. According to a source familiar with Yucaipa's investments, by the fall of 2008, Burkle had almost $7 billion on hand—and an urgent desire to spend it.

One Sunday that October, he invited six senior staff members to La Jolla for an eight-hour conference. "Everybody was afraid the world was coming to an end," says Burkle. "I wasn't. I said, 'This is an opportunity. We can buy phenomenal companies and brands at ridiculous prices.' A lot of times my people can overrule me. Not this time."

Burkle wanted to invest one-third of Yucaipa's money right away. Among the companies that piqued his interest were Whole Foods Market, a seeming relic of a more prosperous era, and Barnes & Noble, whose bookstores were already under threat from e-readers.

When considering Whole Foods, Burkle's 40-person team conducted pricing surveys, met with suppliers, talked to customers, visited stores, and undertook the kind of exhaustive study that might seem unnecessary for someone who grew up in the grocery business. Burkle, though, doesn't trust his gut. "I don't pay attention to how I feel about anything," he says. "What I like or use is irrelevant. I may still wear s----y khakis and these shirts, but I know I'm not in consumers' heads. I don't know what's going on in America. I know what people in New York and Beverly Hills think about Whole

(TOP, L TO R) CHRIS RATCLIFFE/BLOOMBERG; LORENZO CINIGLIO/POLARIS; FABRICE COFFRINI/AFP/GETTY IMAGES; JOEL RYAN/AP PHOTO; MARY ALTAFFER/AP PHOTO; LUCAS JACKSON/REUTERS/CORBIS; JIN LEE/BLOOMBERG NEWS; TIM BOYLE/GETTY IMAGES; DANIEL ACKER/BLOOMBERG NEWS; JEFF ZELEVANSKY/BLOOMBERG NEWS

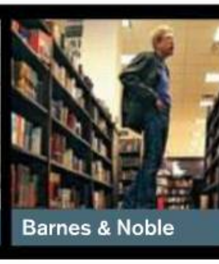
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THE INVESTMENTS


Bono


Sean "Diddy" Combs


Barneys


Barnes & Noble


Whole Foods



A&P

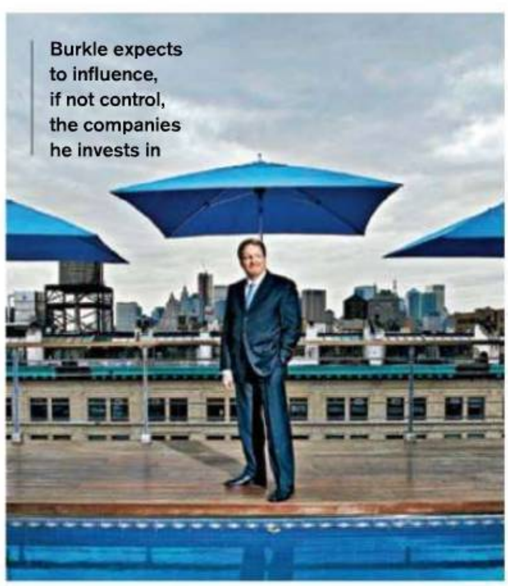
Foods, but I don't know what people anywhere else think."

Yucaipa's research showed that Whole Foods' customers weren't ready to abandon the place, even if some of its prices were unaccountably high. Throughout the autumn and winter of 2008, Burkle bought Whole Foods stock, eventually spending $100 million and accumulating close to a 10% stake. Burkle won't discuss his thoughts on Whole Foods' strategy, but according to sources close to Yucaipa, he advocated opening fewer stores, improving logistics, offering more house brands, and doing bigger promotions. Whole Foods CEO John Mackey has done some of this. In the past several months, as the company's fortunes have improved and its stock price has increased, Burkle has sold almost all of his shares. Yucaipa says its return was about 200%.

Before investing in Barnes & Noble, Burkle and his team asked publishers, book agents, consumers, and tech companies the same question: In the era of the e-book, what good is a bookstore? What Burkle learned was that Barnes & Noble has a deep and abiding relationship with its customers and could do a lot more to exploit it. By January 2009, he had an 8.3% stake and felt entitled to write a few letters to Riggio, another self-made man. "In the first letter," says Burkle, "I said, 'You've had such a successful career, you've made so much money. Don't do the college book deal'"—a reference to Riggio's plan to sell his college textbook company to Barnes & Noble for nearly $600 million. "The letter wasn't supposed to be threatening. It didn't mean I was going to declare jihad."

The company went ahead with the deal, and in November Riggio asked the board to adopt a provision that would effectively bar any shareholder from acquiring more than a 20% stake. Riggio and other insiders own 31%; Burkle, who currently has 18.7%, was not pleased. He wrote to Riggio again, asking to buy up to 37%. The answer was no.

Burkle expects to influence, if not control, the companies he invests in. He says he has thoughts about how Barnes & Noble can become more profitable, but his fight with the company isn't about strategy—yet. It's about governance. On Feb. 25, a week after Barnes & Noble dismissed his request to buy more shares, Burkle wrote another, angrier letter to the board: "In denying my request, the Board has, once again, demonstrated that it acts to protect the interests of the Riggio family in maintaining effective control of Barnes & Noble." He concluded by asking to meet with the board members, though pointedly not Len Riggio or his brother, Stephen, the chief executive. Barnes & Noble declined to comment.


Burkle expects to influence, if not control, the companies he invests in

BRAD TRENT

Companies have all kinds of reasons for preventing outside investors from getting too close—from strategic disagreements to concerns about motives. When the investor is Ron Burkle, there's another reason: the stigma of celebrity. Burkle counts Leonardo DiCaprio and Bono among his friends and toured with the Dalai Lama during his last visit to America. He has invested about $50 million in Al Gore's Current TV (Gore says Burkle "is a personal friend and a good friend to the company") and some $75 million in Sean "Diddy" Combs' clothing line. (Burkle is a godfather to Combs' twin daughters.) It is still all too easy to view Burkle as a lightweight, though his friends warn against it. "Barnes & Noble is in contempt of Ron, and that's not a good offense to commit," says Greif. "Most folks live to regret that."

Burkle hasn't had to be particularly patient over the years, and Barnes & Noble and Barneys are testing his resolve. Istithmar World, a Dubai investment firm, acquired Barneys in 2007 for some $900 million. Amid Dubai's financial calamity in November, Burkle bought some of Barneys' debt. Then he wrote a letter to Istithmar proposing to lend Barneys about $50 million and take control of it. "If you can buy Barneys cheap enough and make it work, which Burkle might be able to do, it could go public and be worth a fortune," says Howard Davidowitz, a longtime retail consultant.

Burkle is waiting. "Dubai is in control of the situation," he says. "We're willing to talk to them about anything. But are they focusing on this? Barneys has no money, no chief executive. They should treat it like it's a great asset." A spokesperson for Barneys says: "As a matter of policy, Barneys doesn't comment on speculation."

Burkle thinks of his uncharacteristically high-profile moves on Barnes & Nobles and Barneys as "adapting to opportunities." The companies resent Burkle for being opportunistic. At least they agree on the adjective. | BW |

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Areva's first EPR, in Finland. The project is three years behind schedule

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A HIGH-END BET ON NUCLEAR POWER

Areva CEO Anne Lauvergeon says a bold new reactor design gives the French company an edge over rivals. Now she has to find customers who can afford it

By Carol Matlack

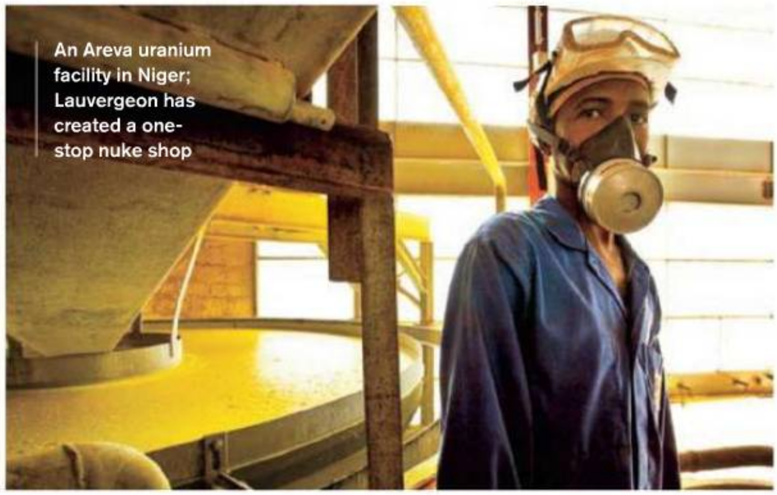
Anne Lauvergeon, chief executive of the French nuclear giant Areva, is getting close to the payoff on a colossal, decade-long bet. In 2001, when she engineered the three-way merger that turned Areva into a one-stop shop selling nuclear technology to the world, many found the idea far-fetched. The U.S. hadn't ordered a nuclear plant since the 1979 Three Mile Island accident. And after Chernobyl in 1986, business dried up just about everywhere outside pro-nuclear France. There are 436 reactors operating in the world today, just 20 more than in 1990. Where would her customers come from?

Undeterred by the nuclear drought, Lauvergeon put Areva's engineers to work on a bold new technology called the Evolutionary Pressurized Reactor. The EPR is super-powerful, fuel-efficient, and loaded with safety features such as a reinforced concrete shell designed, post-September 11, to withstand a direct hit by a jumbo jet. Now the 50-year-old CEO is rolling out the EPR just as the nuclear industry awakens from its slumber. Worldwide, hundreds of reactors are being planned and 53 are being built, three of

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Lauvergeon has been criticized for losing a deal for four reactors in Abu Dhabi



An Areva uranium facility in Niger; Lauvergeon has created a one-stop nuke shop

(L TO R) BRIAN SMALE; JACQUES TORREGANO/FIGAROPHOTO; MAP BY DAVID FOSTER/BW

them EPRs. On Feb. 16, President Obama awarded the first of an expected $54 billion in federal loan guarantees to help U.S. utilities build a new generation of nuclear plants.

At lunch in Areva's executive dining room overlooking the Paris Opera, Lauvergeon predicts the EPR will grab one-third of the global market for new reactors over the next 20 years. That, along with the $11.5 billion company's other holdings—from African uranium mines to factories that turn out everything from fuel pellets to mammoth reactor vessels—will seal Areva's place as the industry's No. 1 player, she insists. "I was always convinced that nuclear had a future," she says between bites of broiled monkfish with chanterelles.

And yet, Lauvergeon may be asked to leave the table before Areva can cash in on its bet. Despite repeated public denials by the government of President Nicolas Sarkozy, French media outlets have reported that she may soon be replaced. Sarkozy has asked former Electricité de France chief François Roussely for a broad review of Areva and the rest of France's nuclear sector, with a report due in April. Meanwhile, trouble is brewing on several fronts. Areva's prototype EPR, under construction in Finland, is three years behind schedule; its cost has gone from $4.1 billion to $7.2 billion. Because Areva agreed to a fixed-price contract, it must eat those overruns, which has sapped profits. Adding to its woes, a contract to supply four reactors to Abu Dhabi slipped through Areva's fingers in December. Korea's KEPCO won the deal with a bid of $20 billion—$10 billion below Areva's. The powerful heads of EDF and French oil group Total, which teamed with Areva in Abu Dhabi, have questioned whether she erred in risking her company's future on a top-of-the-line reactor and not developing a lower-cost option. "You need to have a product line that corresponds to countries' needs," says EDF boss Henri Proglio. Lauvergeon counters that Areva's customers deserve the best available technology.

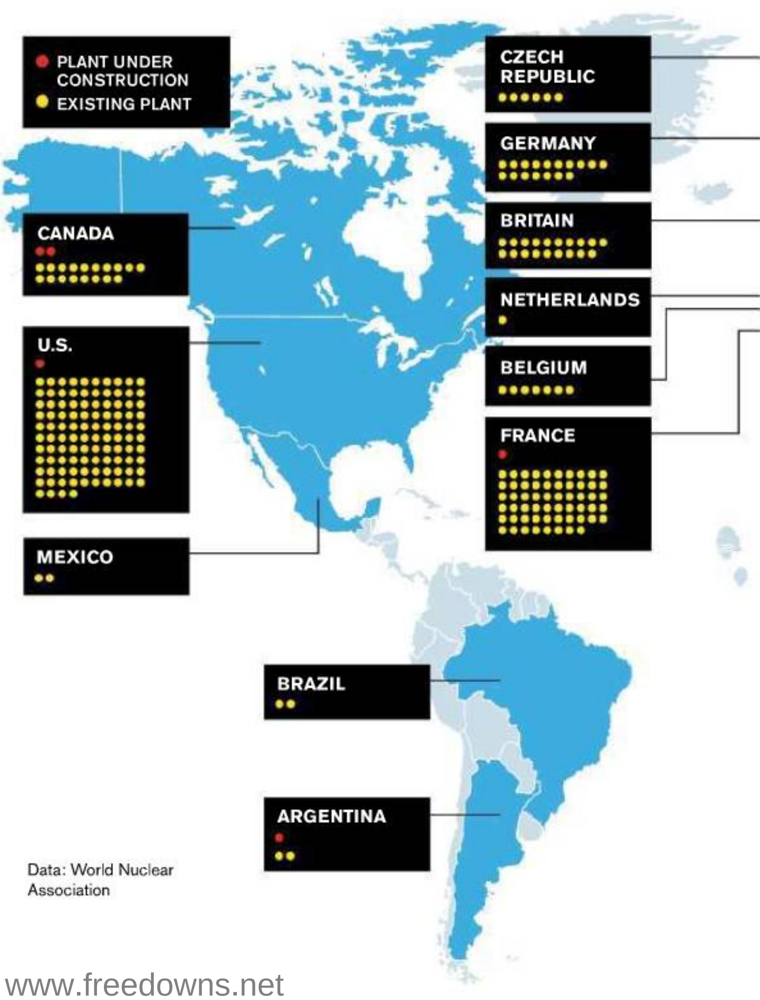
Lauvergeon's difficulties underscore the biggest challenge now facing nuclear power: its price tag. Even as fears about energy independence and global warming have led many policymakers and environmentalists to give nuclear a second look, construction costs for reactors have risen twice as fast over the past decade as those for conventional power plants, according to IHS Cambridge Energy Research Associates. Building a nuclear plant has become a "bet-the-farm risk," ratings agency Moody's says in a report warning that utilities embarking on such projects could face a rating downgrade. Although a government loan guarantee might ease financing concerns, "it doesn't address the big risk"—that regulators won't let utilities jack up rates enough to offset the cost, says Jim Hempstead, a Moody's analyst who oversaw the report.

Why does Lauvergeon remain bullish on nukes? She's certain the technology will have a place in the energy mix even as solar, wind, and other alternatives take off. And Areva has a head start on its chief rivals, Westinghouse Electric and a partnership between General Electric and Hitachi. Both have new reactors with advanced safety features. But they haven't yet built any, while Areva can benefit from lessons learned on EPRs under construction in Finland, France, and China.

For a close-up look at the EPR, visit the Normandy village

A NUCLEAR RENAISSANCE

Utilities worldwide are currently building 53 new reactors. Hundreds more are planned.



Data: World Nuclear Association

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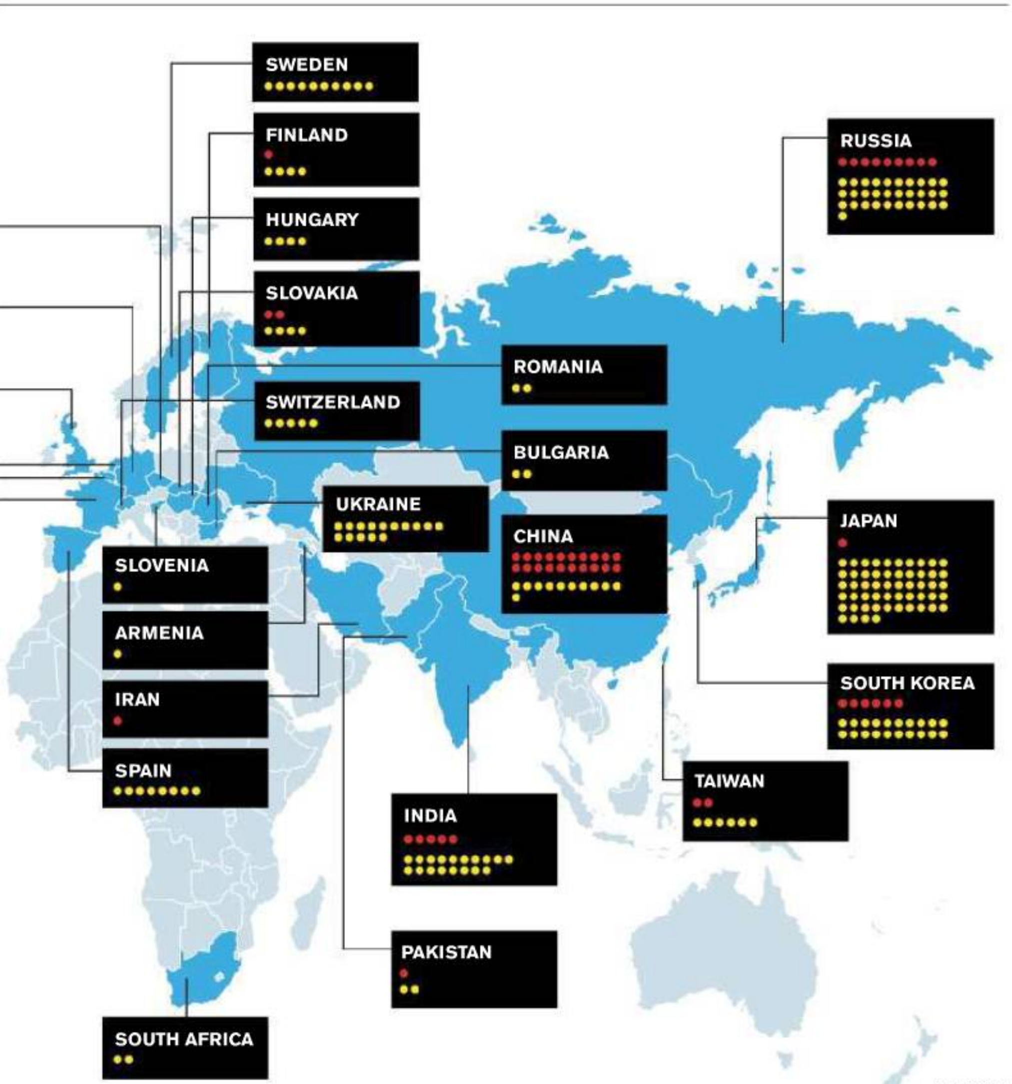
of Flamanville, where Electricité de France is building one. At the foot of a windswept cliff overlooking the English Channel, workers in fluorescent yellow vests pour concrete into molds bristling with reinforcing rods for a circular wall that will encase the new reactor. The containment structure will include enough steel to build half an Eiffel Tower and about twice the concrete of existing nuclear plants.

Such souped-up safety features were key in convincing Baltimore-based Constellation Energy Group to go with an EPR for an expansion of its Calvert Cliffs plant in southern Maryland. The company is in advanced talks to obtain federal loan guarantees, with an eye toward opening the facility by 2015. Despite the cost, some $10 billion, "once that investment is made, we'll have a highly reliable plant," says Michael J. Wallace, Constellation's chief operating officer.

Lauvergeon has used keen political and marketing instincts to keep Areva's U.S. growth on track. Fluent in English, she regularly meets with U.S. industry groups and politicians in states where Areva operates. Last July she joined then-Virginia Governor Tim Kaine to break ground on a joint-venture factory, with Northrop Grumman, to supply components for U.S. plants built by Areva and others. To garner support for the EPR among potential subcontractors, Lauvergeon organized "supplier days" last year in Maryland and Ohio. And last summer she invited high school students from Idaho—home to a planned Areva uranium enrichment plant—to visit similar facilities in France. Compared with its rivals, "Areva is more attuned to the public relations side of things," says Adrian Heymer of the Nuclear Energy Institute, a trade group in Washington.

Still, the U.S. is likely to see less than 10% of the industry's growth over the next decade. China and India, which account for nearly half of the reactors now under construction, are a tougher sell. China has ordered two EPRs, but it also plans to buy four reactors from Westinghouse. And both Areva and Westinghouse have only minority stakes in joint ventures with Chinese partners, which will probably lower profits in China. Like the Chinese, the Indians are eager to develop their own reactor designs, limiting opportunities there, too. In other emerging markets, Areva faces a big challenge from Korea's KEPCO and Russia's Rosatom, which have sold reactors far more cheaply than Areva.

Lauvergeon is ready for the fight. Trained as a physicist at the elite Ecole des Mines de Paris, she worked at the French atomic energy agency in the 1980s before joining the staff of former President François Mitterrand, where she scouted international trips. She then became a partner at Lazard Frères in New York. In 1999, then-President Jacques Chirac tapped her to run Cogema, a state-owned nuclear fuel business. While most countries had halted nuclear construction, France built dozens of reactors during the 1980s and 1990s.



Dismayed by what she calls the French industry's "bunker mentality," she persuaded Chirac to fuse the state's nuclear holdings into a single company, with the government retaining a majority stake. Her plan put Areva in prime position to capitalize on the renaissance, says Roger W. Gale, a veteran U.S. nuclear consultant. Customers are drawn to Areva because, unlike rivals GE and Westinghouse, "nuclear is the only thing they do," Gale says. "They live and breathe it."

Even so, Lauvergeon is hedging her bets. In February she bought Ausra, a California solar startup, and she has added wind and biomass to Areva's portfolio. Renewables today account for only about $1 billion of Areva's $58 billion order backlog, but Lauvergeon says the company someday could get more than a third of its revenues from such activities. More important, at least for now, Areva controls 40% of the profitable market for nuclear fuel and does a brisk business selling generators, replacement parts, and management services to utilities worldwide. "Even if there were zero construction" of reactors, she says, "we would live very well." |BW|

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HOW COLLEGES ARE BUYING RESPECT

By Daniel Golden
Illustration by David Plunkert

For-profit education companies are scooping up small schools to gain accreditation—and the financial aid dollars that come with it

ITT Educational Services didn't pay $20.8 million for debt-ridden Daniel Webster College in June just to acquire its red-brick campus, 1,200 students, or computer science and aviation training programs.

To ITT, the third-biggest higher-education company in the U.S., the Nashua (N.H.) college's "most attractive" feature was its regional accreditation, says Michael Goldstein, an attorney at Dow Lohnes, a Washington firm that has long represented the Carmel (Ind.) company. Regional accreditation, the same gold standard of academic quality enjoyed by Harvard, is a way to increase enrollment and tap into the more than $100 billion the federal government pays out annually in financial aid.

The nation's for-profit higher-education companies have tripled enrollment, to 1.4 million students, and revenue, to $26 billion, in the past decade, in part through the recruitment of low-income students and active-duty military. Now they're taking a new tack. By exploiting loopholes in government regulation and an accreditation system that wasn't designed to evaluate for-profit takeovers, they're acquiring struggling nonprofit and religious colleges—and their coveted accreditation. Often their goal is to transform the schools into taxpayer-funded behemoths by dramatically expanding enrollment with online-only programs; most of those new students will receive federally backed financial aid, which is only available at accredited colleges.

"The companies are buying accreditation," said Kevin Kinser, an associate professor at the State University of New York at Albany who studies for-profit higher education. "You can get accreditation a lot of ways, but all of the others take time. They don't have time. They want to boost enrollment 100% in two years."

By acquiring regional accreditation, trade schools and online colleges gain a credential associated with traditional academia. Six nonprofit regional associations set standards on financial stability, governance, faculty, and academic programs. Normally the process takes five years and requires evaluations by outside professors. Most for-profits have been accredited by less prestigious national organizations. Students enrolled at both regionally and nationally accredited colleges can receive federal aid, but those at regionally accredited schools can transfer credits more easily from one college to the next.

"CREATIVE ARRANGEMENTS"

For-profit education companies, including ITT and Baltimore-based Laureate Education, have purchased at least 16 nonprofit colleges with regional accreditation since 2004. The U.S. Education Dept., which doled out $129 billion in federal financial aid to students at accredited postsecondary schools in the year ended Sept. 30, is examining whether these kinds of acquisitions circumvent a federal law that requires a two-year wait before new for-profit colleges can qualify for assistance, says Deputy Education Under Secretary Robert Shireman. Under federal regulations taking effect on July 1, accrediting bodies may also have to notify the Education Secretary if enrollment at a college with online courses increases more than 50% in one year. "It certainly has been a challenge both for accreditors and the Department of Education to keep

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up with the new creative arrangements that have been developing," Shireman says.

Buying accreditation lets the new owners immediately benefit from federal student aid, which provides more than 80% of revenue for some for-profit colleges, instead of having to wait at least two years. Traditional colleges are also more inclined to offer transfer credits for courses taken at regionally approved institutions, making it easier to attract students.

The regional accreditors, which rely on academic volunteers, bestow the valuable credential with scant scrutiny of the buyers' backgrounds, says Barmak Nassirian, associate executive director of the American Association of Collegiate Registrars & Admissions Officers in Washington. While accrediting bodies treat these purchases as changes of ownership, the acquisitions, in reality, create new colleges that should be required to earn certification from scratch, Kinser says.

For accreditation to continue once the college is sold, the buyer must promise not to change its mission, says Steven Crow, former executive director of the Chicago-based Higher Learning Commission, the largest regional accreditation body. Once accreditation is maintained, the acquirer seeks permission, which is usually granted, to start branch campuses and online programs.

Obama Administration officials have recently questioned whether the present accreditation system is effective in protecting academic standards. Accrediting decisions lack transparency and take too long, Education Under Secretary Martha Kanter said in a Jan. 26 speech.

A BARGAIN

Regional accreditation is worth $10 million to a for-profit acquirer, says Michael Clifford, an education investor in Del Mar, Calif., who has participated in purchases of four nonprofit colleges. That's how much it would cost to start a regionally accredited college, a process that can take 10 years and has only a 50-50 chance of success. On top of the $10 million, buyers typically pay $23,000 to $50,000 per enrolled student, making ITT's purchase of Daniel Webster a bargain, Clifford says.

Clifford and his fellow investors popularized the strategy in 2004 by purchasing Grand Canyon University, a Christian college in Phoenix. Enrollment has soared to 37,700 as of Dec. 31, up from 1,500 students, with 92% taking classes online. Grand Canyon, which went public in November 2008, derived 82.5% of its revenue from federal financial aid in 2009, according to a company filing.

A 2006 regulatory change fostered online growth and made takeovers more attractive. That year, Congress eliminated a rule prohibiting colleges that offered more than half of their courses online from receiving federal financial aid.

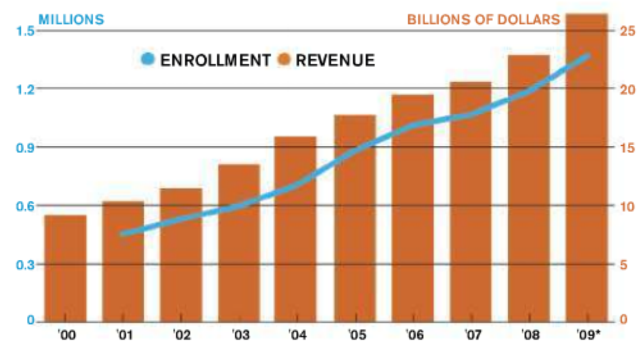
Clifford also participated in the 2008 purchase of Myers University in Cleveland, which was renamed Chancellor University. Chancellor attracted former General Electric CEO Jack Welch as an investor last year and named its new online management institute after him. Welch collaborated with faculty in developing curricula for a master's program in business administration, Clifford says. "We chose to work with Chancellor University because it gave us the flexibility to start something new," Welch said through a spokeswoman. "As a for-profit venture, we have the resources to invest in the student experience and the very best faculty." Knowledge Universe Learning Group, chaired by junk-bond pioneer Michael Milken, entered into a partnership in 2007 with regionally accredited Sierra Nevada College in Incline Village, Nev., agreeing to provide up to $15 million in return for an opportunity to share in online revenue, according to Geoffrey Moore, a senior adviser to Milken.

The regional associations scrutinize takeovers of nonprofit colleges in advance and then follow up afterward, accrediting officials say. They could recall few, if any, cases in which they refused to continue accreditation.

Corinthian Colleges' past difficulties with California state regulators didn't matter to accreditors when it agreed last October to purchase Heald Capital, parent company of Heald College, for $395 million. Corinthian, the country's seventh-largest higher-education company by market capitalization,

BIG MONEY ON CAMPUS

For-profit colleges have tripled both their enrollment and revenue since 2000



has more than 100 campuses in North America, and had 106,052 students, including Heald, as of Dec. 31.

Corinthian had paid a $6.5 million settlement in July 2007 to the California attorney general's office over allegedly misrepresenting graduates' job placement rates and salaries. It also agreed to cease enrolling students in 11 programs at nine campuses. Corinthian, based in Santa Ana, Calif., didn't admit wrongdoing.

The Accrediting Commission for Community & Junior Colleges in Novato, Calif., which certifies two-year institutions in California and Hawaii, approved the change in Heald's ownership. "We judge the college we accredit," says Barbara Beno, president of the commission. "It would be unfair to say, 'Heald, you've been bought by a parent corporation that doesn't have as fine a track record as you do. Therefore, we'll condemn you.'"

That "doesn't remotely satisfy the sloppiest of due-diligence requirements," says Nassirian of the American Association of Collegiate Registrars & Admissions Officers. "There is no methodical review of who has bought the college. If the Cosa Nostra applied, you would think you'd take a look."

The Higher Learning Commission, which certifies more than 1,000 colleges from Arkansas to Wisconsin, stiffened its rules on ownership changes last year. Buyers must wait anywhere from one to four years to reapply for accreditation



(FROM TOP) BACKGROUND BY DAVID PLUKERT; CHART BY STANFORD KAY

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if the college won't remain "the same animal," says President Sylvia Manning. The commission now charges a $10,000 fee for ownership changes to pay for more extensive research, and new owners must be approved by its board rather than at the staff level.

Last year, Mayes Education acquired the assets of Waldorf College, in Forest City, Iowa, an Evangelical Lutheran college with 500 students. The commission, applying its revised rules, stipulated as a condition of approval that Waldorf can't offer online-only degrees at least until the 2011-12 academic year. Mayes, a subsidiary of Columbia Southern University in Orange Beach, Ala., plans to boost Waldorf's enrollment to 2,300 students in three years through programs combining online classes with face-to-face instruction at temporary sites around the country, says company spokeswoman Jessica Brown.

Columbia Southern wasn't the only for-profit that expressed interest in buying Waldorf, says Richard Hanson, Waldorf's former president. Another company that lacked regional accreditation also contacted him: ITT Educational Services.



70%

Amount of revenue ITT derived from federal financial aid in 2009.

Data: ITT Educational Services

ITT runs 120 nationally accredited technical institutes with 80,000 students, most of whom pursue associate's degrees. The cost of attending an ITT Technical Institute, including tuition, fees, and off-campus room and board, was $26,775 in 2008-09, according to the National Center for Education Statistics. Of students who entered ITT's two-year schools in 2004, 29% graduated. ITT derived 70% of its 2009 revenue from federal financial aid.

ITT Educational Services, which declined to comment for this story, is in the preliminary stages of seeking regional accreditation for its technical institutes through the Higher Learning Commission, which sent a team to visit the company last fall, according to commission spokeswoman Susan Van Kollenburg. The commission has not yet acted on this evaluation, she says.

Daniel Webster is ITT's first regionally accredited campus. It was founded in 1965 as the New England Aeronautical Institute. Over the years the college expanded from flight instruction into training air-traffic controllers and airline managers, as well as computer science, engineering, and business. It has "a longstanding good reputation," said Gary Kiteley, executive director of the Aviation Accreditation Board International in Auburn, Ala., which licenses the college's aviation programs.

With an endowment that peaked at about $3 million in 2008, Daniel Webster relied on tuition revenues, says Robert Myers, the school's former president. The airline industry's downturn after the September 11 terrorist attacks and the collapse of Internet stocks hurt enrollment in aviation and computer science, says former provost Michael Fishbein.

Myers says he was contacted by ITT in December 2008. CEO Kevin Modany visited Daniel Webster the next month, and the parties reached agreement in April. New England accreditor Commission on Institutions of Higher Education approved the sale that same month. "It's in the public interest to have these small institutions continue to function," says Bruce Mallory, a commission member and education professor at the University of New Hampshire. "If a proprietary school can come in, continue to provide the same level of education, and assure viability, that's all for the better."

SECOND THOUGHTS

As Myers negotiated the sale, he says, he came to suspect that the company wasn't being forthright. When he and Rodney Conard, who chaired the college's board of trustees, worked out at a YMCA a week before the June closing, they discussed canceling the deal, Myers said. Conard says going through with the sale was the right decision.

According to Myers and Fishbein, Modany promised to leave Daniel Webster's administrators in charge. At a campus event introducing the ITT CEO to the college community, Modany promised there would be ample employment opportunities. In July, ITT laid off more than 20 Daniel Webster employees, Myers says. It believed they were duplicating functions that ITT's corporate offices in Indiana could provide, two people familiar with the company's thinking said. ITT also replaced Conard and the other trustees.

At the time of the layoffs, Myers was circulating a draft report questioning whether some of ITT's changes were in accord with the standards of the accreditation commission, which call for a faculty role in curriculum and governance. "ITT came in and said, 'We only want faculty to teach,'" Myers says. "We'll develop curricula in Carmel, Ind., and give them to you." On Aug. 5, ITT ousted him, he says. Nadine Dowling, director of the Woburn (Mass.) campus of ITT Tech, became interim president.

"ITT didn't really have much interest in anything other than having acquired a regionally accredited institution," says Myers, now president of the New England Culinary Institute in Montpelier, Vt. "If I had it to do all over again, I wouldn't have gone anywhere near ITT. The fundamental nature of the college has changed." Modany declined to comment.

Like other acquirers of regionally accredited colleges, ITT plans to expand Daniel Webster's online offerings. The company also expects to open more Daniel Webster campuses and to introduce new academic programs including accounting, education, and health sciences. "Regional accreditation was very important" to the company, said Goldstein, the Dow Lohnes lawyer. "I don't think there's any question that was the most attractive element." |BW|

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WHAT'S NEXT

STRATEGY & COMPETITION

Privatize This!

Wall Street firms planned to pump billions into infrastructure. A lot of them hit roadblocks

By Jason Kelly and Jonathan Keehner

For years, states and cities around the country have been using duct tape and baling wire to patch over a gargantuan problem: They don't have nearly enough money to maintain their transportation systems, electrical grids, ports, and other crucial facilities. The gap between what governments are likely to spend on infrastructure and what is needed over the next five years, according to the American Society of Civil Engineers, is a mind-numbing $1.1 trillion.

That's why it seemed like good news a few years ago when Wall Street came calling. Kohlberg Kravis Roberts and other big private equity firms talked about privatizing highways and parking facilities, and snapping up utilities, airports, and other infrastructure. They would funnel billions into the nuts and bolts of everyday life, getting access to stable operations that would throw off steady income streams.

KKR launched its infrastructure fund in 2008, citing a "multi-trillion dollar" market opportunity. Blackstone Group, Citigroup, Deutsche Bank, and others piled in. So far, though, KKR has yet to announce any major investors for its fund, much less do a deal. Other firms haven't fared a whole lot better.

As private equity firms waded into public projects, overly optimistic projections and high leverage led to a string of failures. "Aggressive operating and financial assumptions, in times when debt was cheap, resulted in acquisitions that had little or no pricing discipline and didn't work for investors," says Dunia Wright, head of U.S. and Europe for Industry Funds Management, an Australian firm that oversees $19 billion.

At the same time, there has been public backlash against Wall Street buying up Main Street. In Chicago, for example, Mayor Richard Daley faced sharp criticism last year after leasing 36,000 parking meters for 75 years to an investor group led by Morgan Stanley. The profit-minded new operators quadrupled some meter rates and eliminated free parking on Sundays—moves that provoked outrage from drivers and local officials. "Putting us against the investment banks in a deal like that is like having little leaguers play the New York Yankees," says Alderman Thomas Allen of Chicago's 38th Ward, who proposed an ordinance requiring a mandatory 15-day review period for similar agreements.

"PUTTING US AGAINST THE INVESTMENT BANKS IS LIKE HAVING LITTLE LEAGUERS PLAY THE NEW YORK YANKEES"





The marriage of private equity and infrastructure has worked better outside the U.S., since Sydney-based Macquarie Group pioneered the concept of raising money from private investors to buy roads and utilities. To cite just one example, Global Infrastructure Partners, created by Credit Suisse and General Electric, has been running London City Airport successfully since 2006; last year it took over Gatwick Airport.

In the U.S., private equity firms began to focus on infrastructure in 2005, after Chicago turned over a 7.8-mile elevated road known as the Chicago Skyway to a group that included a Macquarie-managed fund. The 99-year, $1.8 billion agreement, the first major privatization of an existing U.S. highway, led to a surge of infrastructure fund raising that peaked at $34.3 billion in 2007, according to consulting firm Probitas Partners.

The flood of capital produced a series of missteps on land, sea, and in the air. In 2007, Deutsche Bank acquired Maher Terminals, which operates shipping facilities in Port Elizabeth, N.J., for its North America Infrastruc-

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(Clockwise from top) Maher Terminals in New Jersey; Chicago parking meters; a Connecticut rest stop; London City Airport

(CLOCKWISE FROM TOP LEFT) BENJAMIN LOWY; JOHN GRESS/REUTERS/CORBIS; BENJAMIN LOWY; CHRIS RATCLIFFE/BLOOMBERG NEWS

ture fund, paying $2.1 billion. Deutsche Bank planned to sell its interest to outside investors. But as shipping activity plunged amid the worldwide recession, the bank had trouble finding takers.

OFF THE RAILS

Deutsche took a charge of $205 million after shifting Maher Terminals in 2008 to its corporate division from its group that manages alternative assets. Executives can now check on their unwanted acquisition by gazing across the water to New Jersey from the windows of Deutsche Bank's U.S. headquarters in downtown Manhattan.

"Investing in infrastructure can't be just a financial play," says Stephen Mentzines, head of Maquarie Capital Funds in North America. "It takes sector expertise and the ability to operate assets."

In early 2009, Chicago cancelled plans to lease Midway Airport for 99 years when a group of investors including Citigroup failed to raise financing. A Fortress private equity fund ran off the tracks when it paid $3.5 billion for Florida East Coast Railway in 2007. It was counting on the Florida state legislature to fund the development of a rail corridor running between Jacksonville and West Palm Beach—but the funding hasn't come through. Fortress has done better with its $450 million investment in Florida's RailAmerica, however.

KKR and Blackstone say they remain committed to making infrastructure investments. And federal stimulus efforts may give Wall Street a chance to find its footing. The Transportation Dept. is set to receive $4 billion to help create a so-called infrastructure bank that would "effectively leverage non-federal resources, including private capital," according to the budget President Obama submitted to Congress in February.

Rude experience may have taught private equity firms better ways of doing these deals. In November, Carlyle Group's infrastructure fund inked a $178 million public-private partnership to manage 23 service areas along Connecticut's highways for 35 years. Carlyle didn't use any leverage, and it worked to win the support of state departments of transportation and environmental protection, as well as community groups and labor unions.

Carlyle managers say it may serve as a model for future transactions. "A lot of people have come to talk to us about it," says Robert Dove, co-head of Washington-based Carlyle's infrastructure group. "There continues to be a real interest in bringing the private sector in." |BW|

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Can Sex and Saucy Ads Sell Chryslers?

The company is retooling—so get ready for Dodges that look like Fiats and TV spots with Gallic sizzle

By David Welch

Sex appeal has virtually disappeared from American car marketing. So when models wearing metallic minidresses shared a stage with a Chrysler concept car at the Detroit Auto Show in January, some onlookers declared the display passé and even déclassé. Olivier François, the impeccably dressed Frenchman in charge of Chrysler's latest rebranding effort, was merely bemused. "I am doing here what I know from [home]," he said.

Chrysler is turning European again. This time, it's not the Germans calling the shots, as they did during Chrysler's short-lived marriage to Daimler. Now the Italians from Fiat and their French marketing chief are in charge, and the next generation of Chryslers and Dodges will resemble the quirky little cars that zip around Rome. François, meanwhile, is willing to push buttons with his marketing—even at the risk of offending prim American sensibilities.

The product and branding makeover amounts to a screeching U-turn for an automaker best known for the Town & Country minivan, the gangsterish Chrysler 300, and the macho Dodge Ram pickup. But CEO Sergio Marchionne badly needs to attract a younger, hipper, wealthier customer as Chrysler's traditional buyers age and dwindle in number. Chasing the same people would be a "dead-end road," says Alexander H. Edwards, president of Strategic Vision, a San Diego consumer research firm. At the same time, Edwards acknowledges "it's a big step to go after a different buyer."

1.1 million

Number of vehicles Chrysler says it needs to sell in the U.S. to make money. This year the company is on pace to sell just 900,000.

Data: Chrysler

The task falls to François, 48, who has a record for marketing stunts that generate controversy. For example, François can be pointedly political, something American car companies avoid (except of course for feel-good flag-waving). In 2008, Fiat apologized to China after a European Lancia ad starring Richard Gere obliquely backed an independent Tibet. Last December, a Chrysler ad that aired on U.S. television featured Mikhail Gorbachev, Poland's Lech Walesa, and Mohammed Yunus, who founded microlender Grameen Bank. Each man climbs out of a 300 sedan, and a fourth car arrives empty. An announcer dedicates the ad to jailed Burmese democracy activist Aung San Suu Kyi.

The spot was a remake—an Italian ad agency simply swapped out the original car, a Lancia Delta—and François could justifiably argue that he was getting good value for money. That didn't stop the carping. In an *Advertising Age* story, former Chrysler marketer Julie Roehm said most Americans wouldn't know who Suu Kyi is. The article quoted other critics who said it was inappropriate for Chrysler to use an Italian agency for the work when the U.S. government owns 10% of the carmaker. François later posted a note on the company's Web site: "Hopefully readers in a democratic society [can] decide for themselves if they should be upset."

Dodge won't get its complement of Italian-style models for at least two years. In the meantime, François is trying to generate new heat around the brand's muscle cars. Exhibit A: the slyly sexist commercial for the Dodge Charger that ran during the Super Bowl. Called "Man's Last Stand," it featured closeups of regular guys (voiced by *Dexter* star Michael C. Hall) saying: "I will shave. I will carry your lip balm. I will put the seat down." The commercial ends with a Charger speeding away as Hall intones: "Because I do this, I will drive the car I want to drive."

"AN EASY TARGET"

François was looking for buzz, and he got it. Several women created parodies of the ad on YouTube. Independent filmmaker MacKenzie Fegan made one called "Woman's Last Stand." It features women saying things like: "I will put my career on hold to raise your children. I will diet, botox, and wax everything." Fegan says that she was "mildly offended by the ad" and that its blunt message and simple format made it "an easy target."

This isn't the first time Chrysler has tried to be edgy. In the early 2000s a commercial featured a mother telling her daughter she was named Concordia because she'd been conceived in their Concorde sedan. "Some people like the Concorde for its engaging style," the tagline went. "Others just like its really big back seat." Another spot featured a reference to wife-swapping. After receiving complaints, Chrysler eventually tweaked the campaign. Roehm was forced to cancel a Super Bowl event dubbed the



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Lingerie Bowl, during which scantily clad women were to play football. In a promotional video, François says he's looking for cars "people want to make out in." But he says he will not go near the kind of controversy generated by Chrysler in the past.



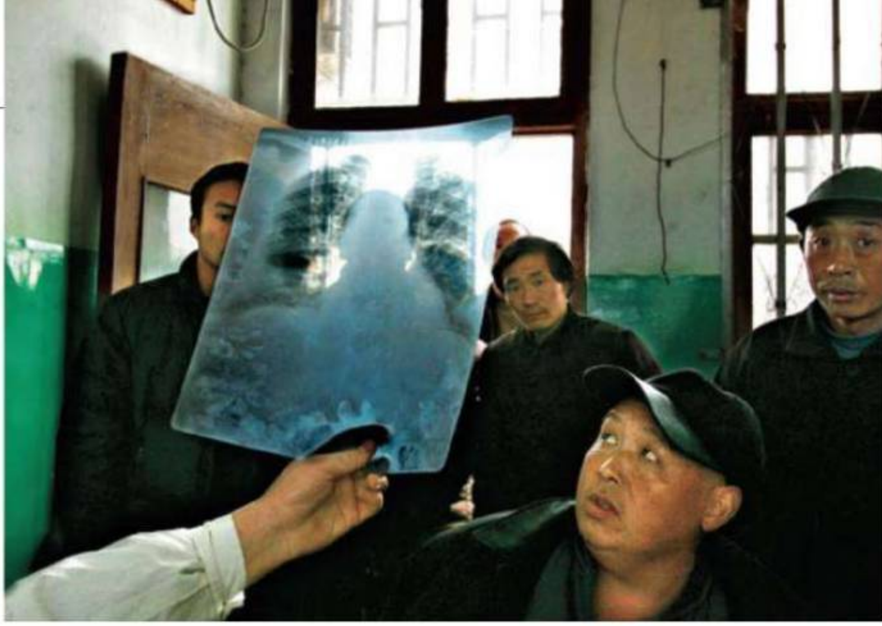
Marketing chief François, left, brings a whole new sensibility to Detroit

Irreverence may get people talking about Chrysler, Dodge, and Jeep again. Much harder is appealing to the broad range of people who still buy cars from these brands without alienating one group or another. Dodge will require a particularly delicate dance. About three-fourths of its buyers are men, and Dodge steward Ralph Gilles wants to attract more women. He recently began running an online ad in which a guy kicks his girlfriend out of their apartment and begins throwing her belongings out the window. Among them are the keys to her Charger, which she starts up and drives away. This spring Chrysler plans to start running family-friendly commercials aimed at soccer moms and dads.

Fiat's Chrysler rehabilitation strategy has attracted plenty of skeptics. Marchionne likes to point out that he turned around Fiat when they said it couldn't be done. Then, he and François were marketing to nationalistic Italians who were craving decent cars. "Fixing Chrysler won't be as easy," says IHS Global Insight analyst John Wolkonowicz. "Americans don't have that kind of loyalty." |BW|

(L TO R) JUAN CARLOS JONES/CONTRASTO/REDUX; DANIEL ACKER/BLOOMBERG

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Much of the new money will go to rural hospitals like this one in Shenqiu County

STEPHEN VOSS/REDUX

STRATEGY & COMPETITION

The Ka-Ching in China Luring Medical Giants

GE, Siemens, and others are angling for a piece of the $125 billion Beijing plans to spend on health care

By Frederik Balfour

As China's leaders move ahead with a $125 billion, three-year plan to improve health care, foreign companies are lining up to get a share of the bounty. The three-year effort includes funding for some 31,000 new hospitals to be built by 2012, mostly in rural areas. With so much new building, "there's a good opportunity to upgrade technologies so they can treat more complex diseases," says Marcelo Mosci, CEO of GE Healthcare China.

The Chinese market for medical equipment will grow an average of 13.5% a year, to $15.5 billion in 2012, the health-care unit of Philips Electronics says. And China's drug market will hit $110 billion by 2015, up from $44 billion in 2008, estimates brokerage Credit Suisse.

$110 billion

China's pharma market in 2015, up from $44 billion in 2008

Data: Credit Suisse

GE and its rivals are working to create products aimed at rural areas, where most of the hundreds of millions of Chinese without adequate health care live. Siemens Healthcare and Philips both have Chinese labs where they're developing relatively inexpensive imaging equipment. GE Healthcare has 600 engineers working in China, many of them coming up with products such as simple black-and-white ultrasound machines and CT scanners that sell for less than 10% of the price of more complex devices for urban areas. The rural market today makes up less than 10% of GE Healthcare's China sales, but it's growing twice as fast as the company's overall business in the mainland. "Village and county hospitals are moving from primary care to more sophisticated diseases," Mosci says. "We have a pipeline of products dedicated to this segment."

Cities, though, remain a big part of the mix. Last year, China surpassed North America as the biggest market for Philips' most advanced CT scanner, a $2 million machine that provides three-dimensional imaging of the brain. GE says the bulk of its business will continue to be selling sophisticated gear for China's big research hospitals and other facilities in cities. While GE declines to give specifics, its sales in China have been growing at a double-digit pace for the past four years and the company expects them to top $1 billion in 2010.

Pharmaceutical companies are hoping to benefit from the health-care plan, too. Beijing has drafted a list of 307 drugs that all hospitals and clinics must stock at fixed prices. Switzerland's Roche and Novartis will both see China revenues grow as many of their drugs are on that list as well as a broader roster of medications eligible for reimbursement by insurers. London-based AstraZeneca plans a big push in rural areas, where it says sales are likely to climb by 20% annually for the next five years. One big winner from the essential drugs list: Betaloc, a hypertension medication that represents 16% of AstraZeneca's revenues in China. "The potential sales are going to be huge," says Yin Xudong, the company's China president.

The foreign companies will face growing competition from domestic rivals. Drugmaker Jiangsu Hengrui Medicine has 70 products on the essential drugs list, and Nanjing-based Simcere Pharmaceutical Group has a dozen, including antibiotics and an anti-stroke medication. Shenzhen-based Mindray Medical International says sales by government tender—mostly of lower-tech devices aimed at rural areas—doubled last year, to $51 million, as overall revenues jumped by 25%, to $293 million. State spending, says Chief Financial Officer Ronald Ede, "has definitely helped us accelerate our sales growth." |BW|

–With Yidi Zhao in Beijing

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ECONOMICS & POLICY

Congressman Calculator

GOP up-and-comer Paul Ryan scares colleagues with doomsday math about Social Security and Medicare



CHRIS USHER

By James Rowley

When numbers are the political weapon of choice, the Republicans turn to Paul Ryan to do their fighting. In prepping for the Feb. 25 televised health-care showdown with President Barack Obama, it was Ryan, a representative from southern Wisconsin's rolling hills and industrial enclaves, who was tasked with challenging the math of the Administration's $2.3 trillion health-care overhaul. At 40, and already on his sixth term, Ryan has the right mix of freshness and experience for the moment. In 2006 he leapfrogged past 13 more senior colleagues to become the House Budget Committee's ranking Republican. Now he's on a mission to spark serious debate about entitlement spending that he argues will "swallow us alive" if left unchecked.

Ryan feels the urgency of the problem so strongly that he isn't afraid to touch the third rail of American politics. In a recently revised 2008 proposal, he suggests partially privatizing Medicare and Social Security, the two biggest entitlements, to prevent their insolvency and curb debt. Not everyone agrees with him. And while Ryan predicts Armageddon on entitlements, he would eliminate income taxes on corporations, capital gains, and dividends, and retain all the Bush-era tax cuts set to expire this year—moves that could set the deficit zooming. But no one questions that his expertise is hard-earned. "I don't think anybody in the entire U.S. Congress knows budget implications and processes better than Paul," says Texas Republican Jeb Hensarling, one of his allies among House conservatives.

Ryan learned to mix numbers and politics from the late Jack Kemp, a fiscal conservative whose views on social issues were sometimes to the party's left. He went to work for Kemp at think tank Empower America when he was 23. Following the Kemp model, Ryan has voted to bar job discrimination against gays and counts as friends three of Wisconsin's Democrats: Senator Russ Feingold, whose family has been close to Ryan's for three generations; Representative Ron Kind, with whom he has teamed up to promote hunting and land conservation; and Representative Tammy Baldwin, the openly gay lawmaker whose district is next to his. "I am not a hater," says Ryan. "Jack Kemp was my political mentor, and I always thought that's the right approach and style—passionate about your beliefs but not insulting to people because they have beliefs that differ from yours."

Ryan's entitlements plan, "A Road Map for America's Future," would keep the current Medicare and Social Security system for people age 55 and older. Younger Americans could personally invest a third of their Social Security payroll taxes and, when Medicare-eligible, get an annual payment to buy private health insurance.

Ryan says safety net spending will "swallow us alive"

After he offered the latest version of the plan at a Jan. 27 news conference, House Speaker Nancy Pelosi described it as the GOP budget that "ends Medicare as we know it." House Republican Leader John Boehner quickly reminded reporters that the plan is Ryan's, not the GOP leadership's.

Pelosi's jibe aside, Democrats are often among Ryan's biggest admirers. Obama praised the plan as a "serious proposal." House Budget Chairman John Spratt Jr., a South Carolina Democrat, calls his proposals "really gutsy" because they "hit some important constituencies right between the eyes."

Ryan says his job is to sound the warning of impending fiscal doom. "What if you knew your congressman knew the timing, scope, nature, and cause of that financial crisis well ahead of time, in time to stop it, but chose not to because it wasn't good politics for him? You'd want to fire that guy." |BW|

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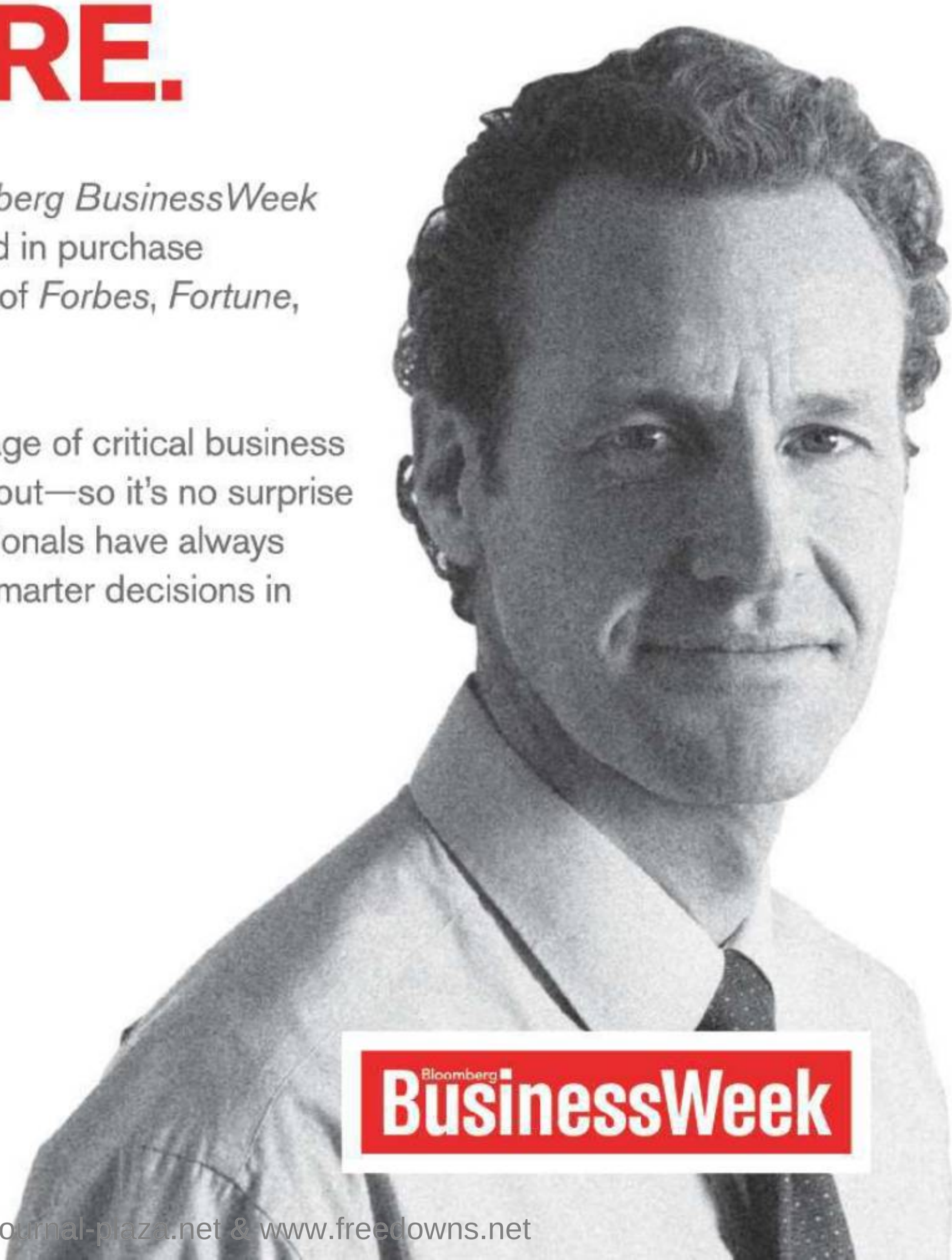
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JACK BLACK

BEST UNDERGRADUATE B-SCHOOLS

With Jobs Scarce, B-Schools Get Creative

Career help is key in *Bloomberg BusinessWeek*'s annual ranking of undergraduate business programs

By Geoff Gloeckler

When the Class of 2010 enrolled in college four years ago, majoring in business seemed the best route to securing a plum job at graduation. Seniors were graduating with two and three job offers, starting salaries averaged close to $50,000, and big signing bonuses and benefits packages were typical. Then came the Great Recession. Students returned from summer internships without job offers. And those lucky enough to land a position had to settle for lower salaries than they had expected.

Many 2009 graduates were still

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searching for work long after they stored their caps and gowns in their parents' attics. Now, as the Class of 2010 prepares to follow them into the workforce, the job market continues to deteriorate. "This year isn't going to be particularly strong," says Edwin W. Koc, director of research at the National Association of Colleges & Employers. "It may be even slightly worse than last year."

Anxiety about jobs, and students' dissatisfaction with the help they are getting from school placement offices, are reflected in *Bloomberg Business-Week's* fifth annual ranking of undergraduate business programs. Only 38% of college seniors majoring in business who responded to our survey in January reported having a job offer in hand. That compares with 46% in 2009 and 56% in 2008. Of the 27,317 student respondents, 58% voiced concern about their job searches and 38% reported they are considering alternatives, such as graduate school or the Peace Corps.

At the top of our ranking is the University of Notre Dame's Mendoza College of Business. In a year when unemployment was at the forefront of student concerns, Notre Dame fared well, thanks in part to a large alumni base willing to lend a hand to young job seekers. At No. 2 University of Virginia's McIntire School of Commerce, students lauded the intense core curriculum taught by teams of professors from different disciplines. Rounding out the top three is the Massachusetts Institute of Technology Sloan School of Management, up four spots from 2009. More than 90% of Sloan students boast summer internships, and its graduates' median starting salary, $62,000, is the highest in the ranking.

WITH THE JOB MARKET SO DICEY, MORE STUDENTS ARE CONSIDERING GRAD SCHOOL, OR MAYBE THE PEACE CORPS



JONATHAN R. WILLIS

Bloomberg BusinessWeek used nine measures to rank these programs, including surveys of senior business majors and corporate recruiters, median starting salaries for graduates, and the number of alumni each program sends to top MBA programs. We also calculated an academic quality rating for each program by combining average SAT scores, student-faculty ratios, class size, the percentage of students with internships, and the number of hours students devote to classwork.

While student satisfaction is down 14% from 2009, the level of discontent varied widely from school to school. Schools that performed well in the ranking pulled out all the stops to help students find work—enlisting faculty and alumni, using social media, and developing talent pipelines to local businesses.

"IT WAS SCARY"

One school that worked hard to find jobs for students was No. 16-ranked Miami University in Oxford, Ohio, where a course designed to provide students with hands-on training is also giving them exposure to prospective employers. When Miami University senior Sarah King, 21, returned to campus after an internship at General Electric without a job, she was terrified. "Even the best and brightest students weren't getting hired," King says. "It was scary." She enrolled in a class called Human Capital Metrics, which pairs groups of students with corporations to help solve problems the companies are facing. King was paired with Nestlé. As her team's liaison with the company, King was in weekly contact with Laura Warren, a Nestlé recruiter.

Throughout the semester, Warren observed King's work habits and business skills. "I got to see the quality of Sarah's work," Warren says. "We had three months with her, not just a 30-minute interview." When Warren began interviewing students for full-time positions, she was certain that King would be a good fit. And King, having learned about the company, was better prepared than most candidates. In the end, she got a job and will start work in August.

At the No. 15-ranked Robins School of Business at the University of Richmond, alumnus Paul B. Queally has stepped in to make sure the school's students are well prepared when it comes to the interview process.

Queally has seen hundreds of job candidates come into his office without any clue about how to present themselves. "They aren't really buttoned up," says Queally, co-president at New York-based private equity firm Welsh, Carson, Anderson & Stowe. He wanted to make sure Robins students didn't make the same mistakes. So in

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Miami University's King benefited from a class that linked her directly with Nestlé

early 2008, under Queally's guidance, Robins launched a program called Q-Camp. The two-day crash course aimed at sophomore business students covers everything from the one-minute elevator pitch and networking to thank-you notes and business dinner etiquette. Presenters at Q-Camp include job placement officers, recent graduates, and recruiters. In January nearly 100 Robins students registered for the program, up from 30 last year. The training, says Queally, "gives Richmond students a potential advantage in the interview process where they compete with candidates from Ivy League schools."

Elsewhere, schools are using technology to give their students an advantage. At Virginia's McIntire School, Tom Fitch, assistant dean of career services, has taken to the Web, using Twitter and Facebook to distribute career tips and help find jobs and internships for students, particularly in industries where few openings exist. Says Fitch: "We're really trying to be creative in our whole approach."

TWEETS AND VIDEO

Through his Twitter page, Fitch is able to send out tweets of any career information that he thinks his students might find useful. Recent tweets include a link to 50 common interview questions and a blog post on how the job market will improve—in 2014. In the social media world, competitors sometimes become allies, with career services officers from one school sharing tips and job leads with colleagues at other programs. But that's O.K., says Fitch, who has more than 900 Twitter followers: "We're all out for the same goal, which is helping students find jobs."

Similarly, students at Notre Dame are being taught to use tech tools to connect with alumni working in specific industries. In the hopes of getting more students in front of recruiters, the school has started using Skype's video capabilities for virtual interviews so companies don't have to spend the money to travel to campus. In less than three weeks, six companies have taken the school up on its offer, scheduling nine video interviews.

Even in the best of times, enticing recruiters to campus is never easy. Like many schools, No. 6 Haas School of Business at the University of California at Berkeley has seen a considerable falloff in recruiter traffic on campus—30% for the 2008-09 academic year. There's little a school can do to goose those numbers, so Tom Devlin, director of the career center, did the next best thing: He figured out a way to make the most of the recruiters who do visit.

Devlin's team came up with what he calls the Turn the Tables Fair. Unlike a traditional career fair, where employers set up booths and pitch their companies to students, student groups, such as the finance or marketing club, take the lead, selling themselves to passing recruiters. It's a more targeted way for recruiters to reach interested students, and for students to connect with the right companies. More than 50 student clubs and 45 employers took part in the first fair last fall. "The feedback was phenomenal," Devlin says.

In a better economy, this kind of outreach probably wouldn't be necessary. But to help business students from the Class of 2010 succeed, undergraduate B-schools are considering every available option. **| BW |**

THE TOP TEN

A deteriorating job market for new college graduates caused widespread dissatisfaction among students this year. Schools that succeeded in finding jobs for grads rose to the top of the ranking.

2010/2009 RANK	SCHOOL	ANNUAL TUITION & FEES*	MEDIAN STARTING SALARY	FACULTY-STUDENT RATIO	AVERAGE SAT SCORE	TEACHING QUALITY GRADE**	JOB PLACEMENT GRADE**
1 / 2	Notre Dame (Mendoza) Notre Dame, Ind.	$38,477	$55,000	18.5	1411	A+	A+
2 / 1	Virginia (McIntire) Charlottesville	9,872	55,500	10.2	1370	A+	A+
3 / 7	MIT (Sloan) Cambridge, Mass.	37,782	62,000	1.8	1457	B	A
4 / 3	Pennsylvania (Wharton) Philadelphia	38,970	60,000	11.1	1450	A+	A+
5 / 8	Cornell Ithaca, N.Y.	21,814	55,000	18.2	1402	A+	A+
6 / 6	UC Berkeley (Haas) Berkeley, Calif.	10,333	55,000	18.1	1400	B	A+
7 / 9	Emory (Goizueta) Atlanta	38,036	53,000	9.5	1364	A+	A+
8 / 4	Michigan (Ross) Ann Arbor	11,645	59,000	15.6	1356	B	A+
9 / 17	Boston College (Carroll) Boston	39,130	55,000	26.0	1345	A	A+
10 / 10	Texas (McCombs) Austin	9,808	54,000	34.0	1286	A+	A+

Data: *Bloomberg BusinessWeek*, Cambria Consulting *For in-state students ** Based on 2010 student survey

BUSINESSWEEK.COM | For the complete ranking, plus a slide show, interactive table, methodology, and profiles of all 111 ranked programs, go to businessweek.com/business-schools/

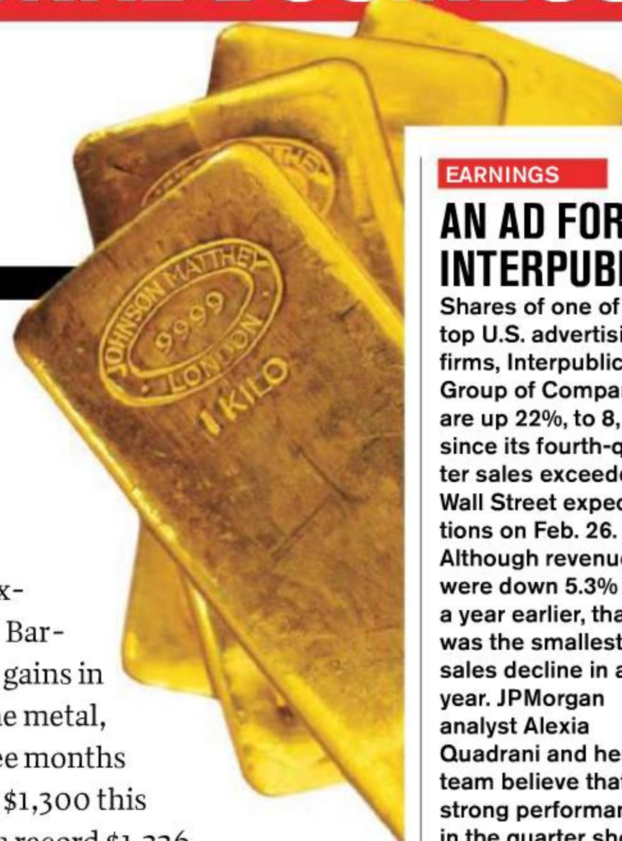
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PERSONAL BUSINESS

MONEY REPORT

GOLD GAIN?



George Soros has helped drive up gold prices by more than doubling his bet in a market even he calls a "bubble." Soros Fund Management, which oversees about $25 billion, increased its investment in SPDR Gold Trust, the world's largest exchange-traded fund for gold, by 152% in the fourth quarter, a Feb. 16 Securities & Exchange Commission filing shows. Goldman Sachs, Barclays Capital, and HSBC Holdings all predict more gains in gold before any bubble bursts. Goldman expects the metal, trading around $1,113 an ounce, to hit $1,235 in three months and $1,380 in 12 months. HSBC says it may peak at $1,300 this year. While prices have fallen 8.2% since reaching a record $1,226 on Dec. 3, 15 of 22 analysts in a Bloomberg survey see gold reaching a new high, with the median forecast predicting a 15% advance to as much as $1,300 an ounce in 2010. Gold is up about 22% in the past 12 months and the same amount since the start of the third quarter, when Soros accumulated 2.44 million shares of SPDR Gold Trust. *–Nicholas Larkin and Pham-Duy Nguyen*

THE STOCK MARKET

RISK RIDDLE

Prices in the options market show that investing in U.S. stocks is getting safer—or do they? The Chicago Board Options Exchange Volatility Index (VIX), which measures the expected volatility of the S&P 500, notched its third consecutive weekly drop on Feb. 26, to 19.5. The gauge has averaged 20.3 since 1990 and moves in the opposite direction of stocks more than 80% of the time. While volatility has fallen in 2010, the probability of wider price swings is up: The cost of buying an options contract that protects against a drop in the S&P 500 over the next two years has risen to the highest level since November 2007, a month after U.S. stocks peaked. Such bearish options cost 1.42 times as much as contracts that are a bet on the stock market rising. That's one of the highest readings in five years. A bearish Mohamed El-Erian, co-chief investment officer for bond giant Pacific Investment Management, says falling volatility means government spending masks a stagnating economy that will keep returns below average. *–Lynn Thomasson, Rita Nazareth, and Jeff Kearns*

80%

Percentage of time the VIX Index moves in the opposite direction of the S&P 500

Data: Bloomberg

EARNINGS

AN AD FOR INTERPUBLIC

Shares of one of the top U.S. advertising firms, Interpublic Group of Companies, are up 22%, to 8, since its fourth-quarter sales exceeded Wall Street expectations on Feb. 26. Although revenues were down 5.3% from a year earlier, that was the smallest sales decline in a year. JPMorgan analyst Alexia Quadrani and her team believe that the strong performance in the quarter shows that "weakness in ad spending is moderating." Interpublic CEO Michael Roth says he detects "encouraging signs on the spend side, and of course General Motors is back to spending." Part of the firm's improving results stem from how "management was more aggressive [than peers] in reducing costs," according to a Mar. 1 Jefferies & Co. report. Credit Suisse analyst Peter Stabler noted in a report on Feb. 28 that Interpublic's stock could trade as high as 10 within 12 months. *–Tara Kalwarski and Brett Pulley*

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INVESTING

Q&A: MUTUAL FUNDS

THE CASE FOR CONVERTIBLES

Convertible bonds trounced the rebounding stock market in 2009, with the Merrill Lynch All Convertibles All Qualities Index returning 49.1% to the S&P 500's 26.5%. Investors noticed, and assets flowed into convertible bond mutual funds. Calamos Convertible, one of the oldest and best in the field, saw assets more than quadruple, to more than $3 billion.

Is there any upside left for those who missed out? In an interview with reporter Laura Lallos, fund manager John Calamos Sr., 69, argues that convertibles remain attractive. The bonds pay interest but also can be exchanged for shares of stock. If the stock goes up, so does the price of the bond; if the stock goes down, the coupon provides a cushion. An example: While Intel's stock fell 36% during the last four months of 2008, its 1.5% convertible bond maturing in 2011 lost 12%. The Calamos Convertible Fund, which held the bond, lost 21.6% for the period, vs. the S&P 500's 29% fall.

With an annualized 4.5% return over the past 10 years through Feb. 23, Calamos Convertible has outperformed the S&P 500, which lost 0.4%, and the Merrill Lynch index, which gained 1.9%. Since John Calamos is concerned about the U.S. economic outlook, Calamos Global Growth & Income may be even more desirable—with half of its portfolio in convertibles, it has one of the strongest 10-year risk-adjusted records among world stock funds.



MICHAEL L. ABRAMSON

What is the case for convertibles?
Convertibles are still undervalued. They went down more than they should have in 2008 [as hedge funds liquidated], so the rebound was partly closing that valuation gap. New issuance in 2009 also created plenty of opportunities.

So much money has gone into the bond market, yet inflation may be right around the corner. I started in this business in the 1970s, when inflation cratered the bond market and the equity markets went sideways for more than a decade. Convertibles ended up being the best-performing asset class.

The highest-yield bonds did best last year. Were you tempted to dip down in quality?
Such a strategy would have worked out very well last year, but downside safety is important to us, so we avoid the most speculative issues.

How should investors allocate convertibles within their portfolio?
We position them as a defensive equity strategy. We aim to achieve 75% of the upside of equities with 25% of the downside. If you like dividend-paying stocks, you're going to love convertibles. On average, you will get twice the income, maybe more, and still have upside potential if stocks keep going up. And you have relatively moderate interest-rate risk.

Are foreign convertibles more attractive than domestic now?
After what has happened over the past couple of years, we recommend investors think more globally than ever before. The last time we found ourselves facing inflation and economic and political uncertainty, in the 1970s and the early '80s, there was no place else to go because it was difficult to invest outside the U.S. Not that we are negative about the U.S. per se, but there are good opportunities overseas. Of course, there is sovereign risk; consider Greece. But if one government is wrongheaded, the financial markets will punish it and the flows will go elsewhere.

Does Calamos Convertible have foreign exposure?
It will have some foreign exposure, but it is U.S.-centric. Calamos Global Growth & Income invests in stocks and convertibles around the world. It has 37% in Europe, 34% in the U.S., 7% in Canada, 9% in emerging Asia, plus stakes in other emerging markets. I think the global convertible market will give us more opportunities. | BW |

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INVESTING

OUTLOOK: STOCKS

WHY TECH HAS ROOM TO RUN

By Tara Kalwarski

The S&P 500 information technology index rose 61% in 2009, so it's reasonable to ask if, in 2010, tech stocks have anywhere to go but down. Dig into the data, though, and you'll find reason for optimism. Prices are at about the same level they were in early 2008, and after recent boosts in earnings forecasts, the companies trade at about 14.8 times projected earnings, down from 16.9 two years ago.

Last year's tech juggernaut was packed with lower-quality stocks, particularly in semiconductors, that had been battered in the downturn, says Fidelity Select Technology manager Charlie Chai. This year he predicts the leaders will be higher-quality companies "that put up sustainable growth." That outlook assumes a continued economic recovery. If no large bumps in the road emerge, here's how pros think tech stocks will play out.

LEADING THE CHARGE

Tech companies depend on four types of buyers: consumers, businesses, the telecom industry, and governments—each of which has cut back on spending. Consumers remain constrained by job worries, telecom customers are spending less, and government budgets are a mess. That leaves corporations to lead the charge back into tech, says Richard Parower, manager of Seligman Global Technology. Hardware and software companies are most likely to benefit. "A lot of people have outdated equipment and software," says Zachary Shafran, portfolio manager of Waddell & Reed Advisors Science & Technology Fund. Chai sees signs of the pickup in hardware sales and says that a software recovery tends to lag.

Computer companies in the S&P 500 are about 17% undervalued, and software outfits sell at an average discount of about 14%, according to Bloomberg's consensus of analyst forecasts. Those same analysts predict shares of Dell could rise 28% over the next 12 months and software company Compuware could see its stock rise 27%, to 10. Shafran particularly likes Microsoft. "It used to be people bought their products because they had to," he says. "Now [Microsoft products] are actually getting good reviews." At 29, shares are about 22% below their 2007 peak.

EMERGING SPENDERS

Spending outside of the developed world will become even more crucial for tech companies. "China, Brazil, and India will drive the growth," says Parower. He says about a third of his fund is in foreign companies, with 5% in Check Point Software Technologies, an Israeli company that gets more than half of sales from outside the Americas. He also likes Amdocs, a European company that makes software for customer-relationship management and billing and gets about25% of sales outside Europe and the U.S.

And if the global recovery stagnates? Morningstar analyst Toan Tran says to stick with quality: Apple, Hewlett-Packard, IBM, and yes, Microsoft. "If the U.S. economy doesn't do well, none of these companies will go bankrupt because of it." | BW |

TOP TECH FUNDS

These high-rated mutual funds all share one thing in common: Microsoft in the top five holdings.

FUND/TICKER	TOTAL RETURN* 1 YEAR	3 YEARS	5 YEARS	TOP FIVE HOLDINGS
Fidelity Select Technology/ FSPTX	95%	1%	5%	Microsoft, Apple, Google, Oracle, Hewlett-Packard
T. Rowe Price Science & Technology/PRSCX	75%	1%	4%	Microsoft, IBM, Accenture, Qualcomm, McAfee
Seligman Communications & Information/SLMCX	57%	4%	9%	Synopsis, Check Point Software, Microsoft, Amdocs, Symantec
Waddell & Reed Science & Technology/UNSCX	48%	3%	8%	Microsoft, Cree, Alliance Data, Aspen Tech., Research in Motion

*As of Feb. 26; multiyear returns are annualized
Data: Bloomberg, Morningstar

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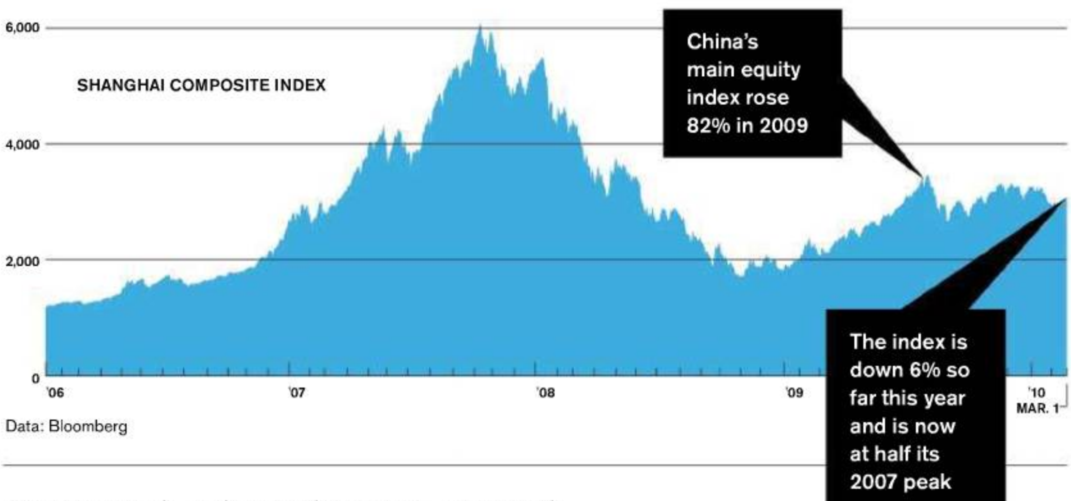
INVESTING

EXCHANGE-TRADED FUNDS

BEAR IN A CHINA SHOP

By Suzanne Woolley and Tara Kalwarski

Could a tap on the brakes in China lead to an equity market skid? The Chinese government's move to head off inflation by reining in bank lending has investors jittery. A billion dollars has flowed out of China equity funds so far this year. That's twice as much as the same period last year (2009 ended with inflows of $5.4 billion). Fund managers are cutting back on commodity producers that feed China's $4.9 trillion economy. Profit-taking could be a factor—China stocks rose 82% in '09. Here's how a shock to the nation's system could affect portfolios.



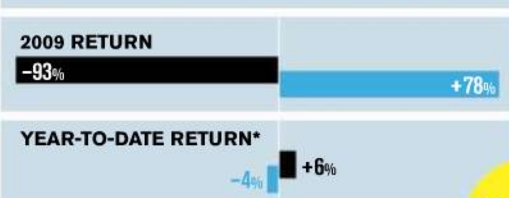
Data: Bloomberg

RUNNING AGAINST THE BULLS

Strong-stomached investors can use these funds to bet on downdrafts in Chinese stocks. But if prices rise, the leverage these funds use would mean even bigger losses.

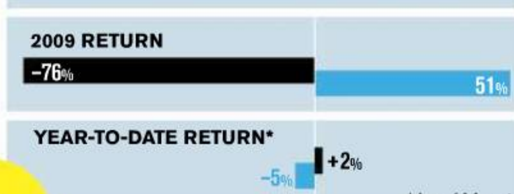
Direxion Daily Emerging Markets Bear 3x EDZ

The goal is to get three times the inverse of the performance of the MSCI Emerging Markets Index, which is about 18% China. Direxion also offers other inverse China exchange-traded funds.



UltraShort FTSE/Xinhua China 25 ProShares FXP

Aims for 200% of the inverse move in an index that tracks the 25 biggest Chinese companies by market cap, including China Mobile (10%) and Industrial & Commercial Bank of China (8%).





*As of Mar. 1

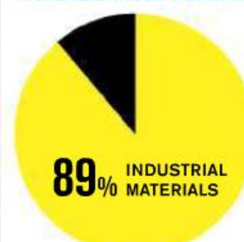
CHARTS BY DAVID FOSTER/BW

COMMODITY CRUNCH

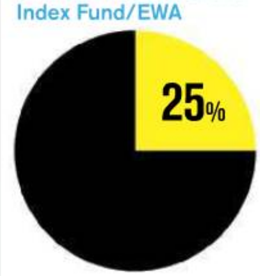
A slowdown in China would hurt sector and country funds heavy in industrial materials. Aussie mining giant BHP Billiton—a top holding in the global materials and Australia ETFs below—gets 20% of sales from China.

FUNDS AND PERCENT OF ASSETS IN INDUSTRIAL MATERIALS

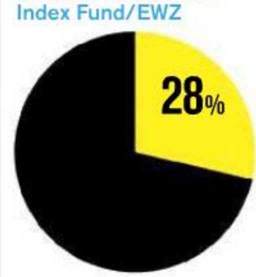
iShares S&P Global Materials Index Fund/MXI



iShares MSCI Australia Index Fund/EWA



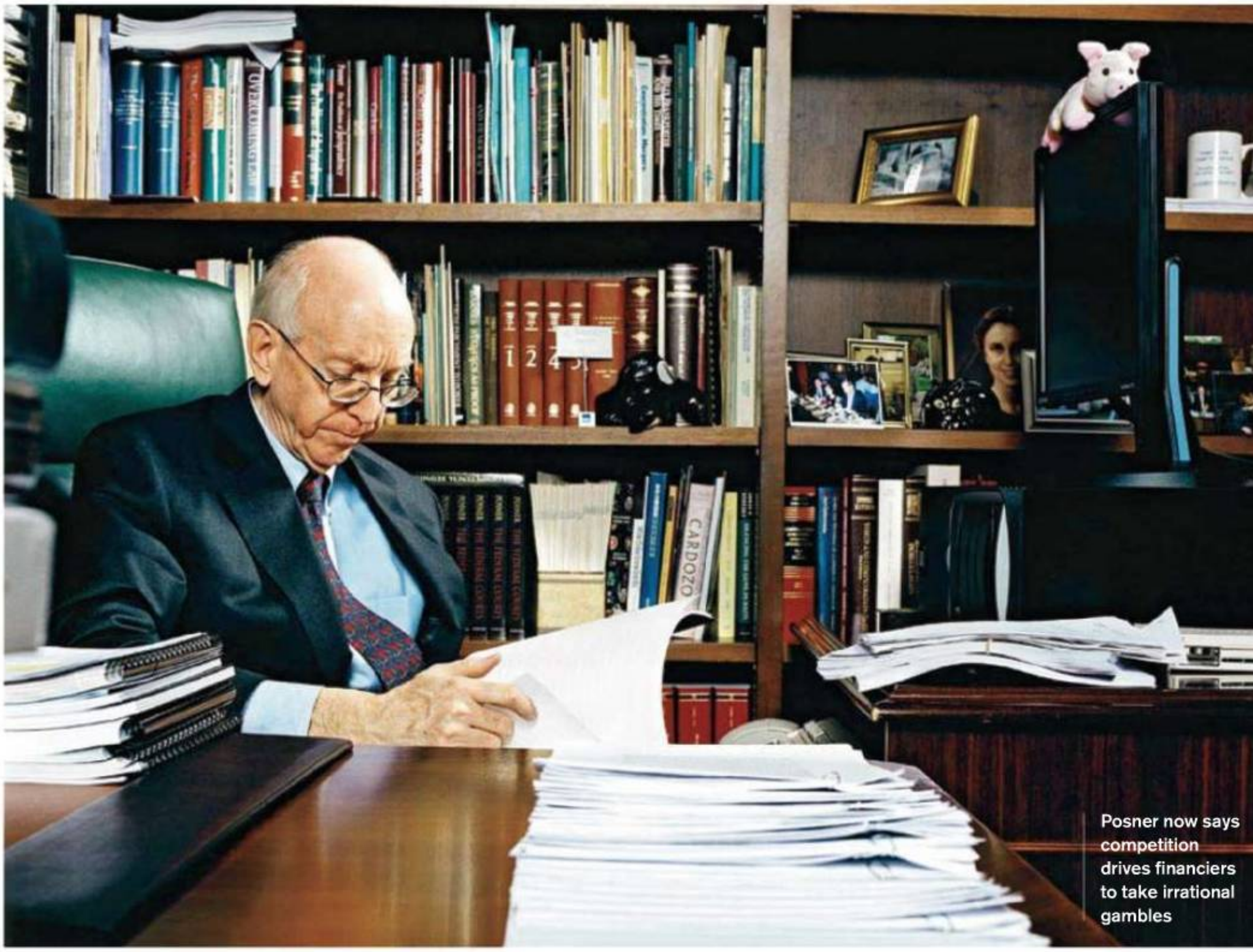
iShares MSCI Brazil Index Fund/EWZ



*Most recently available data as of Feb. 26 Data: Morningstar

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Posner now says competition drives financiers to take irrational gambles

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BOOKS By PAUL M. BARRETT

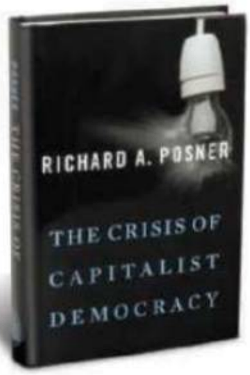
Slapped by the Invisible Hand

Richard Posner has steadfastly fought the regulation of markets—until now

My favorite moment from the so-far listless proceedings of the Financial Crisis Inquiry Commission—appointed by Congress to get to the bottom of this mess—came when Jamie Dimon, CEO of JPMorgan Chase, quoted his daughter to put events in perspective. "My daughter called me from school one day

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and said, 'Dad, what's a financial crisis?' " Dimon told the commission on Jan. 13. "And, without trying to be funny, I said, 'This type of thing happens every five to seven years.' And she said, 'Why is everyone so surprised?' "



I took Dimon's point to be that we ought to follow his daughter's wise example and just calm down. By 2015 at the outside, we'll have another near-Depression experience, and, heck, that's just the way it goes. Certainly the Dimon family has no reason to fret.

It is this type of plutocratic insouciance, combined with the government's flaccid attempts at reform, that led Richard A. Posner to sound the alarm once again. In his latest book, *The Crisis of Capitalist Democracy*, the prolific federal judge and University of Chicago economist argues that competitive forces inspire financiers to take irrational gambles—especially when they're betting other people's money. We cannot trust them to put the common good ahead of profits, says Posner. As a result, government must step in to limit the risks bankers take and, occasionally, repair the damage they inflict.

Posner, who less than a year ago began his dissection of the crisis of 2008 with *A Failure of Capitalism* (Harvard, May 2009), has enormous credibility when he casts a skeptical eye on Wall Street. As an influential free-market thinker, he helped shape the antiregulatory ideology that inspired so much public policy since 1980. Belatedly he admits error. The Chicago School and all its powerful acolytes blundered, Posner writes, "by persuading themselves that markets were perfect, which is to say self-regulating, and that government intervention in them almost always made things worse."

That was a crude misreading of history. Laws inspired by the Great Depression helped achieve a half-century without catastrophic meltdowns. The dismantling of those laws and emasculating of the agencies established to enforce them—without the enactment of new regulation suited to today's Wall Street—go a long way toward explaining our recent brush with disaster.

***The Crisis of Capitalist Democracy* by Richard A. Posner; Harvard; $25.95; 408 pp**

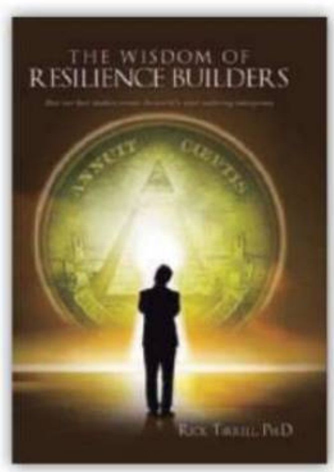
Posner regrets the oversight. He concedes that he personally succumbed to the fallacy of market perfection in some of his writings on solving legal disputes with economic analysis. During the Reagan Administration, those writings made him a candidate for a nomination to the U.S. Supreme Court. One reason he didn't get the nod was that some in Reagan's circle had doubts about Posner's restless intellect, fearing he might prove unpredictable on the high court. Those fears were prescient, it turns out; Posner would have been a fascinating justice to follow.

Today he even tips his hat respectfully toward liberal hero John Maynard Keynes, acknowledging that in the face of consumer and business reluctance to spend in 2009, Washington had to open the fiscal spigots. Posner gives two cheers for the emergency stimulus, judging its size as a good guess in dire circumstance but inveighing against any more stimulus as "irresponsible." He frets about the government's ability to deal with the aftereffects: rising public debt and the temptation to inflate the currency.

His deeper fear, however, is that the political system cannot digest the lessons of the crisis. Society tolerates the inherent recklessness of financial markets, he says, to promote growth and innovation. Although the crash has highlighted the need for regulation, legislators—mesmerized by bankers' campaign cash—seem incapable of passing anything but anodyne reforms.

Posner offers solid suggestions for change. He echoes those, including former Fed Chairman Paul Volcker, who would reestablish the Glass-Steagall Act's separation of commercial banking from proprietary trading and other forms of high-risk finance. That would insulate the financing of small and midsized businesses from the gales of Wall Street. He also urges eliminating the semi-official status of the big three bond-rating agencies, paring back their conflicts of interest, and beefing up the beleaguered corps of civil servants who staff federal regulatory agencies.

Good ideas, all. In his final pages, though, the author can't muster much confidence that America will overcome its splintered politics, the "quasi-bribery" of campaign money, or the bipartisan myth that we can thrive indefinitely on low taxes and profligate public spending. Posner may have shaken off old shibboleths—and hurray for that—but at present he sees no reason to expect that courage or fresh thinking will prevail. |BW|



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TECH & YOU

By RICH JAROSLOVSKY

Behind the Buzz About Mint

The finance site is really Quicken for the short-attention-span generation

In Mint.com's creation story, as recounted on its Web site, founder Aaron Patzer started the free online personal finance service after a tedious session with Intuit's Quicken budgeting software in 2005. It's a measure of Mint's success that any new complaints about Quicken should now be directed to Patzer himself. Tired of getting its clock cleaned by Mint, Intuit bought the site in 2009 and put Patzer in charge of its entire consumer finance operation. He must figure out how all the pieces will fit together—while rejuvenating Intuit's aged Quicken franchise.

Mint's greatest strength is its ability to create a budget for people who don't have the time or patience to make one themselves. It's basically Quicken: Short-Attention-Span Edition. Once you provide log-ins for your bank accounts and credit cards, the site gathers your transactions, categorizes them, analyzes your spending patterns, and says what you have to work with. Surrendering my log-ins didn't bother me. I've been doing that with Quicken for years. But it felt weird to know Mint was looking at my spending habits—much the way I feel knowing Google is analyzing the contents of my Gmail messages to show me ads.

There are two ways of looking at how well Mint performs. On the one hand, it's impressive to have a budget at all, given that Mint constructs it with essentially no input from you. On the other, it sometimes struggled to recognize accounts and transactions. And while it guessed that my purchases at Whole Foods were groceries, it couldn't draw the same conclusion for Kings Super Markets. So what can the user do? You notice the problems, go in, and fix them. In other words: You refine your budget. After a while, you may even find yourself clicking on the Planning tab and beginning to do more serious work on your financial future. The key is that you're doing it on your timetable.



The software also provides a useful companion iPhone app and warns you by e-mail or text alerts if your balance is low or you've exceeded your budget.

Mint makes money collecting bounties from financial institutions for steering you to their products based on your spending patterns. It clearly labels which offers come from its sponsors, and you'll find unsponsored ones mixed in as well. Beware: There's less to some of those "savings" than meets the eye. For instance, Mint recommended a credit card that supposedly would save me thousands of dollars by giving me a bunch of rewards and perks, but failed to consider the perks of my current card. Once I went into my account and added these details, most of the purported savings evaporated.

Making online payments is also beyond Mint's capabilities, and the program lacks powerful investment-management tools. For that you'll still need Quicken, which comes in various editions ranging in price from $29.99 to $89.99, including its first new Mac version in three years.

Frankly, a dash of Mint's youthful DNA would help Quicken. Intuit comes out with new versions of it every year. They're mostly indistinguishable from one another, except when some annoying feature is introduced that you must figure out how to turn off. Quicken also requires frequent updates of dubious value. Release No. 7 to the 2010 edition crippled my ability to download transactions from or send payments through my main checking account.

Quicken is an old workhorse of a program. My father loved it—but he passed away in 1989. For better or worse, Mint.com isn't my father's Quicken. Mostly for the better. |BW|

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PETER ARKLE

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OUTSIDE SHOT

By CLAYTON CHRISTENSEN

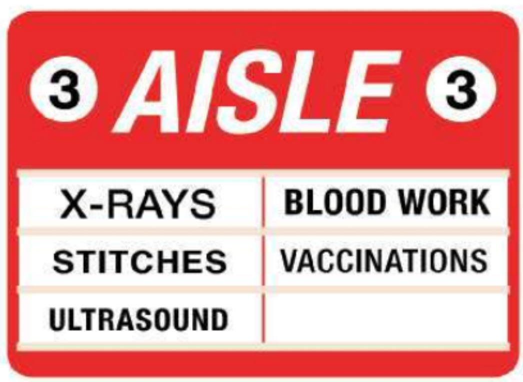
Health Care: The Simple Solution

When it comes to reform, we should drop the public-private debate. The way to cut costs is to put care and insurance in the same bed

I have spent much of my professional life studying innovation. Twelve years ago some friends suggested that the struggles of our health-care system were essentially problems of managing innovation. Instead of studying health care to reach conclusions about health care, as others have done, they suggested examining the industry through the lens of innovation.

Along with two physicians, I recently wrote *The Innovator's Prescription.* My co-authors' work, and my forays into health care—I've had diabetes for 30 years, suffered a massive heart attack, and am now in chemotherapy for lymphoma—informed our perspective. Our key conclusion: The cause of runaway health costs is malpractice, but not the medical kind. Rather, we're guilty of business model malpractice on a grand scale. Most caregivers in our system bring great talent and commitment to their patients. But the systems in which they work compromise quality and push up costs.

Those who debate insurance reform in Washington and pit public against privately funded care are framing the problem incorrectly. Here's a better way to think about it: Economists are wrong in asserting that competition controls costs. Most often innovation and competition drive prices up, not down, because bringing better, higher-priced products to market is more profitable. Hospital-vs.-hospital competition causes providers to expand their scope and offer more premium-priced services. Equipment suppliers boost the capability and cost of their machines and devices. Drugmakers develop products that bring the highest



prices. It's because we have such competition, not because we lack it, that health costs are rising by 10% a year.

The type of competition that brings prices down is disruptive innovation. Disruption in health care entails moving the simplest procedures now performed in expensive hospitals to outpatient clinics, retail clinics, and patients' homes. Costs will drop as more of the tasks performed only by doctors shift to nurses and physicians' assistants. Hoping that our hospitals and doctors will become cheap won't make health care more affordable and accessible, but a move toward lower-cost venues and lower-cost caregivers will.

The public-private divide shows that the debate is stuck at the wrong fork in the road. Many public health systems, like Canada's and Germany's, are departmentalized, with separate administrators handling doctors, hospitals, drugs, insurance, and so on. Although government pays the costs, such public systems are similar to the American system, where employers pay for the services of independent insurers, hospitals, doctors' practices, and drugs. In departmentalized structures, innovations that add costs in one silo in order to save money or improve performance in another cannot succeed because the overall system lacks a unified perspective. Independently managed hospitals have incentives to fill their beds; independent insurers have incentives to minimize reimbursement and access; and the ensuing gridlock prevents all but the most incremental of innovations.

In integrated systems—where the provider and insurer are the same entity—a single perspective enables providers to take actions in one place that will cut costs or lift performance in another. While hospitalization is a revenue opportunity to an independently managed hospital, in integrated systems hospitalization is seen as a failure. Integrated systems, including Kaiser Permanente in California, Geisinger Health System in Pennsylvania, the public systems in Finland and New Zealand, and the Veterans Administration in the U.S., can provide better care at 20% to 30% lower cost. Clearly, systemic problems require systemic solutions.

I desperately hope that our lawmakers in Washington fail to reach agreement on either public or private options because these are wrong answers to the wrong questions. Both will permit perpetuation of the sort of business model malpractice that forces us to pay so dearly for health care and will, in the end, strangle our economy. | BW |

Clayton Christensen is a professor at Harvard Business School and a co-founder of think tank Innosight Institute.

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